(2)

FILED

97 1072 DEC 29 1997

No. _____

OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term 1997

VIRGINIA STATE CORPORATION COMMISSION;
Petitioner,

TEXAS OFFICE OF PUBLIC UTILITY COUNSEL,
Petitioner.

v.

FEDERAL COMMUNICATIONS COMMISSION;
AND
THE UNITED STATES OF AMERICA,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA

Appendix to Petition for Writ of Certiorari

Of Counsel:
Stewart E. Farrar
James C. Dimitri
William H. Chambliss
Robert M. Gillespie*
State Corporation Commission
Office of General Counsel
P.O. Box 1197
Richmond, VA 23218
(804) 371-9671

Counsel for Petitioner
Virginia State Corporation Commission

Suzi Ray McClellan
Rick Guzman*
Eva King Andries
P.O. Box 12397
Austin, TX 78711-2397
(512) 936-7500

Counsel for Petitioner
Texas Office of Public Utility Counsel

* *Counsel of Record*

THE LEX GROUP ♦ 1205 East Main Street ♦ Suite 2 East ♦ Richmond, VA 23219
(804) 644-4419 ♦ (800) 856-4419 ♦ Fax: (804) 644-3256

122 pp

TABLE OF CONTENTS
Appendix to the Petition

D.C. Circuit Court of Appeals decision of July 1, 1997 ..... App. 1

D.C. Circuit Court of Appeals Order Denying Virginia State Corporation Commission's and Consumer Intervenors' Petitions for Rehearing, September 16, 1997 ..... App. 37

D.C. Circuit Court of Appeals Order Denying Virginia State Corporation Commission's and Consumer Intervenors' Petitions for Rehearing In Banc, September 16, 1997 ..... App. 39

D. C. Circuit Court of Appeals, Order Denying Intervenor APCC's Petition for Rehearing, October 7, 1997 ..... App. 41

D.C. Circuit Court of Appeals, Order Denying Intervenor APCC's Suggestion for Rehearing In Banc, October 7, 1997 ..... App. 43

In the Matter of Universal Payphone Corp., Petition for Declaratory Ruling, FCC 85-222 Memorandum Opinion and Order (Released May 6, 1985) Excerpts, ¶¶ 15 and 16 of Discussion ..... App. 45

FCC NOPR, June 6, 1996 Excerpts - ¶¶ 2-23 (without footnotes) ..... App. 47

FCC Report and Order, September 20, 1996
Excerpts - ¶¶ 48-61 (without footnotes)
Appendix D ..... App. 60

Excerpts from United States Code Annotated
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS
CHAPTER 5 – WIRE or RADIO CCOMMUNICATION
SUBCHAPTER I – GENERAL PROVISIONS
Section 151 ..... App. 77
Section 152(b) ..... App. 78
Section 225(a)(1) and (b)(2) ..... App. 80
Section 226(e) ..... App. 82
Section 332(c)(3)(A) ..... App. 84
Section 276 ..... App. 86
Section 501 ..... App. 89
Section 502 ..... App. 89

Virginia State Corporation Commission Petition for Rehearing and Suggestion for In Banc Consideration ..... App. 90

Texas Office of Public Utility Counsel and Consumer Federation of America Petition for Rehearing and Suggestion for Rehearing In Banc ..... App. 101

ILLINOIS PUBLIC TELECOMMUNICATIONS ASSOCIATION, Petitioner,

v.

FEDERAL COMMUNICATIONS COMMISSION and United States of America, Respondents, Competitive Telecommunications Association, et al., Intervenors.

Nos. 96-1394, 96-1395, 96-1407, 96-1428, 96-1429, 96-1466, 96-1476, 96-1478, 96-1479, 96-1482, 96-1484, 96-1485, 96-1486, 97-1016, 97-1021, 97-1022, 97-1039, 97-1048, 97-1069, 97-1070 and 97-1080.

United States Court of Appeals,
District of Columbia Circuit.

Argued: May 13, 1997.

Decided: July 1, 1997.
Entered: July 1, 1997

Telecommunications service providers and state regulatory commissions sought review of Federal Communications Commission (FCC) order revamping regulatory regime for payphone industry pursuant to the Telecommunications Act of 1996. The Court of Appeals held that: (1) Act authorized FCC to set local coin rates for payphones; (2) decision to deregulate local coin rates for payphones was not arbitrary and capricious for failing to address possibility of "locational monopolies"; (3) FCC could set local coin rates according to market forces; (4) decision to set compensation rate for toll-free and access code calls as equal to deregulated local coin rate was arbitrary and capricious; (5) interim compensation plan was arbitrary and capricious; (6) "carrier pays" compensation

scheme for toll-free telephone calls was valid; (7) FCC could require interexchange carriers (IXCs) to "track" calls from payphones; (8) FCC was not required to prohibit all discrimination by particular telecommunications operating companies that provided payphone service in favor their own payphone services; and (9) FCC's method of payphone asset valuation was invalid as to portion of method based on fair market value.

Granted in part and denied in part.

For Supplemental Opinion, see 1997 WL 568761.

[1] STATES
TELECOMMUNICATIONS

Telecommunications Act provision requiring Federal Communications Commission (FCC) to establish regulations ensuring that payphone operators be "fairly compensated" authorized FCC to set local coin rates for payphones and thereby preempt states' power to regulate such rates. Telecommunications Act of 1996, 47 U.S.C.A. § 276.

[2] TELECOMMUNICATIONS

Decision of Federal Communications Commission (FCC) to deregulate local coin rates for payphones was not arbitrary and capricious for failing to address possibility of "locational monopolies" held by certain payphone service providers (PSPs), since FCC did not ignore possibility of problematic monopolies, but, rather, concluded that FCC would deal with them if and when specific PSPs were shown to have substantial market power. Telecommunications Act of 1996, 47 U.S.C.A. § 276.

[3] TELECOMMUNICATIONS

Requirement that Federal Communications Commission (FCC) regulation of intrastate matters be narrowly tailored did not come into play where preemption of state regulation

did not arise by implication, but, rather, FCC was given express statutory authority to take particular action.

[4] TELECOMMUNICATIONS

Federal Communications Commission (FCC) could rely upon market forces to determine local coin rates for payphones, pursuant to Telecommunications Act provision requiring FCC to establish regulations ensuring that payphone operators be "fairly compensated," without making statutory findings on whether "forbearance" from regulating such rates was appropriate; FCC did not forebear from applying any regulation but merely established compensation plan in accordance with Act which was market-based. Telecommunications Act of 1996, 47 U.S.C.A. §§ 160, 276.

[5] TELECOMMUNICATIONS

Decision of Federal Communications Commission (FCC) that compensation rate to be paid to payphone service providers (PSPs) by interexchange carriers (IXCs) for toll-free and access code calls should be equal to deregulated local coin rate for payphones was arbitrary and capricious, even if rate was merely default rate which could be renegotiated by IXCs, because FCC's rationale for decision, that costs of such calls were similar, was contrary to evidence and FCC failed to acknowledge contrary data.

[6] TELECOMMUNICATIONS

Interim plan established by Federal Communications Commission (FCC) for compensation rate to be paid to payphone service providers (PSPs) by interexchange carriers (IXCs) for toll-free and access code calls, which was based on deregulated local coin rate for payphones, was arbitrary and capricious because there was no basis for linking compensation rate to local coin rate and plan required payments from only large IXCs for first year of plan.

[7] TELECOMMUNICATIONS

Failure of Federal Communications Commission (FCC) to provide compensation for "0+" calls, which require caller to dial only "0" plus number caller is trying to reach, or calls from inmate payphones under interim plan to be effective prior to full regulatory scheme promulgated under Telecommunications Act, which required FCC to establish regulations ensuring that payphone operators be "fairly compensated," was arbitrary and capricious, because plan was inconsistent with statutory mandate to ensure fair compensation for every completed call. Telecommunications Act of 1996, 47 U.S.C.A. § 276(b)(1)(A).

[8] TELECOMMUNICATIONS

Telecommunications service providers adequately raised claim before Federal Communications Commission (FCC) that interexchange carriers (IXCs) should compensate payphone service providers (PSPs) for "0+" calls, which require caller to dial only "0" plus number caller is trying to reach, under FCC's interim plan which was to be effective prior to full regulatory scheme for payphone industry that would be promulgated under Telecommunications Act, to preserve issue for judicial review, despite providers' promise not to challenge interim plan on that basis, as promise was conditioned on FCC's provision of some level of recompense for such calls. Telecommunications Act of 1996, 47 U.S.C.A. § 276.

[9] TELECOMMUNICATIONS

Establishment of "carrier pays" compensation scheme for toll-free telephone calls made from payphones was not arbitrary and capricious, as scheme would not preclude competitive market pricing, and scheme was based on balancing of competing concerns of administrative efficiency and consumer convenience, as well as Federal Communications Commission's valid judgment that carriers

were primary economic beneficiaries of such calls.

[10] TELECOMMUNICATIONS

Federal Communications Commission (FCC) did not act arbitrarily and capriciously by requiring interexchange carriers (IXCs) to "track" payphone calls as part of regulatory scheme promulgated under Telecommunications Act, which required FCC to establish regulations ensuring that payphone operators be "fairly compensated," since IXCs had ability to track calls. Telecommunications Act of 1996, 47 U.S.C.A. § 276.

[11] TELECOMMUNICATIONS

Telecommunications Act section providing that particular telecommunications operating companies that provided payphone service were not to prefer or discriminate in favor of its own payphone service did not require Federal Communications Commission (FCC) to prohibit all discrimination by such companies; thus, FCC could proscribe discrimination only in provision of basic services. Telecommunications Act of 1996, 47 U.S.C.A. § 276(a)(2), (b)(1)(C).

[12] STATUTES

In determining whether Congress has spoken directly to particular issue, in evaluating agency's interpretation of statute, court considers not only language of particular statutory provision under scrutiny, but also structure and context of statutory scheme of which it is part.

[13] TELECOMMUNICATIONS

Method set forth by Federal Communications Commission (FCC) for valuing payphone assets which required fair market valuation of those payphone assets transferred to separate affiliate or operating division was arbitrary and capricious, but required use of net book value

for payphone assets not transferred was valid, because operating companies' shareholders bore risk of loss on payphone assets and thus should reap bbenefit of increases in value of such assets, and transactions at issue were not ongoing transactions but were made pursuant to statutory reform. Telecommunications Act of 1996, 47 U.S.C.A. § 276(a)(1), (b)(1)(B); 47 C.F.R. § 32.27(b).

[14] TELECOMMUNICATIONS

Section of Telecommunications Act requiring that payphone subsidies be discontinued did not require that certain operating companies' payphone assets be transferred to its unregulated books, but required only that payphone assets not transferred to separate affiliate be accounted for under nonstructural safeguards designed to effectively protect against cross-subsidization. Telecommunications Act of 1996, 47 U.S.C.A. § 276(b)(1)(B).

On Petitions for Review of Orders of the Federal Communications Commission.

Michael K. Kellogg, Washington, DC, argued the cause and filed briefs for petitioners Bell Atlantic Corporation, BellSouth Corporation, NYNEX Corporation, Pacific Telesis Group, Southwestern Bell Telephone Company and U.S. West, Inc.

Robert F. Aldrich, Washington, DC, argued the cause for petitioners American Public Communications Council, Georgia Public Communications Association and Illinois Public Telecommunications Association, with whom Albert H. Kramer was on the briefs.

Robert M. Gillespie, Associate General Counsel, Richmond, VA, Virginia State Corporation Commission, argued the cause for petitioners Utility Regulatory Commissions of the Various States. With him on the briefs were Lawrence G. Malone, Solicitor, Public Service

Commission of New York, Albany, NY, Jonathan D. Feinberg, Assistant Counsel, Albany, NY, Penny Baker, Patrick S. Berdge, San Francisco, CA, Peter G. Ballou, Augusta, ME, Sheldon M. Katz, Montpelier, VT, Ann E. Henkener, Columbus, OH, George M. Fleming, Houston, TX, and Terrence J. Buda, Harrisburg, PA.

Theodore B. Olson, Washington, DC, argued the cause for petitioners Personal Communications Industry Association, Paging Network, Inc., and Pagemart II, Inc., with whom Scott Blake Harris, Washington, DC, and Robert L. Hoggarth, New York City, were on the briefs.

David W. Carpenter, Chicago, IL, argued the cause for petitioners Interexchange Carriers, with whom Mark C. Rosenblum and Peter H. Jacoby, Basking Ridge, NJ, Genevieve Morelli, Alexandria, VA, Danny E. Adams and Steven A. Augustino, Washington, DC, Michael J. Shortley, III, Arlington, VA, Dana Frix, C. Joel Van Over, Frank W. Krogh, Richard S. Whitt, Washington, DC, Douglas F. Brent, Louisville, KY, Leon M. Kestenbaum, Jay C. Keithley and Harold R. Juhnke, Washington, DC, were on the briefs.

John E. Ingle, Deputy Associate General Counsel, Federal Communications Commission, Washington, DC, argued the cause for respondent, with whom William E. Kennard, General Counsel, Christopher J. Wright, Deputy General Counsel, Laurence N. Bourne, Joel Marcus, Counsels, Joel I. Klein, Acting Assistant Attorney General, U.S. Department of Justice, Robert B. Nicholson and Robert J. Wiggers, Attorneys, were on the brief.

Michael K. Kellogg, Washington, DC, argued the cause for intervenors, the Regional Bell Operating Companies and National Telephone Cooperative Association, with whom L. Marie Guillory and David Cosson were on the brief.

Richard P. Bress, Washington, DC, argued the cause for intervenor Peoples Telephone Company. Maureen E. Mahoney was on the brief.

Robert F. Aldrich, Washington, DC, argued the cause for

intervenor American Public Communications Council, with whom Albert H. Kramer was on the brief.

S. Walter Washington, Eva King Andries, Austin, TX, and Elizabeth A. Noel, Washington, DC, filed the joint brief for intervenors National Association of State Utility Consumer Advocates, et al.

Charles C. Hunter, Washington, DC, and Catherine M. Hannan, Bowie, MD, filed the brief for intervenor Telecommunications Resellers Association.

Before: EDWARDS, Chief Judge, GINSBURG and SENTELLE, Circuit Judges.

Opinion for the Court filed PER CURIAM.

PER CURIAM:

Before us are 20 consolidated petitions seeking review of an order of the Federal Communications Commission revamping the regulatory regime for the payphone industry pursuant to the Telecommunications Act of 1996. The petitions challenge the Commission's decisions to (1) assume authority over the rates for intrastate local coin calls; (2) set the interim rate of compensation to payphone service providers (PSPs) for access code calls and subscriber 800 calls at the market rate prevailing in the majority of states that have deregulated local coin calls; (3) tie the permanent rate of compensation for such calls to the market rate for local coin calls; (4) require only large interexchange carriers (IXCs) to pay PSPs for these calls during the first year; (5) require all IXCs both to track compensable coin calls and to compensate PSPs after the first year; (6) reclassify payphone assets transferred from the regulated to the deregulated operations of a Bell Operating Company (BOC) at net book value and those transferred from a BOC to a separate affiliate at fair market value; and (7) forbid the BOCs from

discriminating between their own and their competitors' PSPs in the provision of tariffed services.

We conclude that the Commission acted arbitrarily and capriciously in selecting the interim and permanent rates of compensation for access code and subscriber 800 calls; in requiring only large IXCs to pay PSPs for these calls during the first year; in failing to provide any interim compensation to PSPs for so-called "0+" calls and calls from inmate payphones; and in prescribing fair market value for payphone assets transferred from a BOC to a separate affiliate. Therefore, we grant in part and deny in part the petitions for review.

I. BACKGROUND

Historically only local exchange carriers (LECs) provided payphone service because its provision could not be accomplished independently from an LEC's network. In the mid-1980s the development of "smart" payphones enabled independent PSPs to begin competing against the payphone operations of the LECs. *See Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Notice of Proposed Rulemaking (NPRM),* 11 F.C.C.R. 6716 ¶¶ 4-6.

Generally speaking PSPs do not own the premises on which their payphones are located; instead, a PSP must contract with the owner of the premises, also known as the "location provider." *See* NPRM ¶ 6. PSPs are compensated for calls made from their phones in two ways. First, they collect coins directly deposited into the payphones. This is the usual method of compensation for local calls. In the states (all but five) that regulate the rates for local coin calls a call costs from $0.10 to $0.35. *Id.* ¶ 19 & n.59. In the states that have deregulated local coin rates, the market rate for a coin call is $0.35 per call in four and $0.25 per call in one. *Id.* Second, each PSP—except those affiliated with a

BOC—is compensated through a contract with an IXC (also known as an operator services provider or OSP) for the provision of operator services for collect calls and for calls billed to a calling card or to a third party. Pursuant to these contracts, the PSP agrees to "presubscribe" its payphones to the OSP for these types of calls; in other words, the OSP is the default IXC for any call made from the PSP's payphones. In exchange, the IXC agrees to pay the PSP a percentage of the revenues it earns from calls made from that PSP's payphones. *Id.* ¶¶ 7, 8. Calls made using the services of the presubscribed OSP are called "0+" calls because the caller simply dials "0" plus the number he is trying to reach. In addition to the above two methods of receiving compensation for calls made from payphones, the payphone operations of LECs also receive a subsidy from the carrier common line charges that the LECs assess the IXCs for originating and terminating long-distance calls. These subsidies place independent PSPs at a significant competitive disadvantage vis-a-vis the LECs' payphone operations. *Id.* ¶ 8.

PSPs receive no compensation for access code calls and subscriber 800 calls. Access code calls are the calls to 800 numbers or 10XXX numbers that the caller uses to reach the long-distance carrier of his choice; all other 800 calls are known as subscriber 800 calls. PSPs used to block callers' attempts to "dial-around" the presubscribed OSP by means of an access code. With the passage of the Telephone Consumer Services Improvement Act (TOSCIA), Pub.L. No.101-435, 104 Stat. 986 (1990) (codified at 47 U.S.C. § 226), PSPs were no longer permitted to block such calls. *See* 47 U.S.C. § 226(c)(1)(B). Because access codes are often 800 numbers, TOSCIA effectively prevented the PSPs from blocking subscriber 800 calls as well. At the same time the Congress authorized the Commission to prescribe the compensation to be paid by the OSPs to the PSPs "for calls routed to providers of operator services" other than the presubscribed

OSP. *Id.* § 226(e)(2). Pursuant to this provision the Commission ordered the OSPs to compensate the PSPs for access code calls but declined to prescribe compensation for subscriber 800 calls. *See Policies and Rules Concerning Operator Services Access and Pay Telephone Compensation*, 6 F.C.C.R. 4736 ¶¶ 34, 36 (1991), recon., 7 F.C.C.R. 4355 ¶ 50 (1992).

It was against this background that the Congress enacted § 276 of the Telecommunications Act of 1996 "to promote competition among payphone service providers," 47 U.S.C. § 276(b)(1), by having the Commission "establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone." *Id.* § 276(b)(1)(A). In addition, the Act forbids a BOC from "subsidiz[ing] its payphone service directly or indirectly from its telephone exchange service operations or its exchange access operations" or from "prefer[ing] or discriminat[ing] in favor of its payphone service." *Id.* § 276(a). The Act also provides that the Commission must

> (B) discontinue the intrastate and interstate carrier access charge payphone service elements and payments ... and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues ...; [and]
>
> (C) prescribe a set of nonstructural safeguards for Bell operating company payphone service ... which safeguards shall, at a minimum, include the nonstructural safeguards equal to those adopted in the Computer Inquiry—III (CC Docket No. 90-623) proceeding.

Id. § 276(b)(1).

The Commission's first task was to determine the scope of its new mandate. The Commission decided that the Act's broad directive to promulgate regulations that would ensure

that PSPs are "fairly compensated for each and every intrastate and interstate call" required the Commission to act only with respect to those types of calls for which a PSP does not already receive fair compensation. *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996* (CC Docket No. 96-128), FCC 96-388 ¶¶ 48-49 (rel. Sept. 20, 1996) (*Order*), *recon.*, FCC 96- 439 ¶ 4 (rel. Nov. 8, 1996) (*Reconsideration*). The Commission found that such calls included local coin calls, access code calls, subscriber 800 and other toll-free calls, and 0+ calls provided by PSPs affiliated with a BOC. *Order* ¶¶ 52-58.

The Commission then decided that the best way of ensuring that PSPs are "fairly compensated" is to let the competitive market set the price for each call. *Order* ¶ 49. Accordingly, the Commission declared that the local market for coin calls would be deregulated except where a particular State could demonstrate that competition would not constrain prices, because, for example, payphones at certain locations could be priced at monopoly rates. *Id.* ¶ 51. In determining the rate at which PSPs should be compensated for access code calls, subscriber 800 calls, and other toll-free calls, the Commission rejected the cost-based approach, which attempts to approximate a PSP's actual cost for each type of call. The Commission instead adopted a "market-based" surrogate for the pricing of such calls—namely, the price for a local coin call at a particular payphone once the rates for such calls are deregulated—stating that the "cost[s] of originating the various types of payphone calls are similar." *Id.* ¶ 70. The Commission emphasized, however, that the local coin rate would be only the default rate, from which the PSPs and IXCs could negotiate a departure; and the Commission expected the IXCs would have "substantial leverage" to negotiate due to their ability to block subscriber 800 calls from any particular PSP's payphones. *Id.* ¶¶ 70-71; *Reconsideration* ¶ 71.

The Commission then had to decide who would pay the new charges for access code calls and subscriber 800 calls. The Commission concluded that rather than have the caller deposit money directly into the payphone for such calls, the IXC should be required to pay these charges, for which it could later bill the caller or the 800 subscriber, respectively. *Order* ¶¶ 17, 83-85. An IXC that did not want to incur charges from payphones charging excessive rates could block such calls from those phones. *Id.* ¶ 17. The Commission also decided to hold the IXC responsible for tracking the number of access code calls and subscriber 800 calls it carries from each payphone in order to determine the amount of compensation it owes each PSP; the Commission found that it is technically feasible for the IXCs to track compensable calls. *Id.* ¶ 96.

The Commission established a two-year interim compensation scheme whereby PSPs not affiliated with an LEC would receive compensation for access code calls and subscriber 800 calls (but not for inmate and other 0+ calls). The interim compensation scheme relies upon the modal rate ($0.35) for a local coin call in the five states that have deregulated the rate for such calls. For the first year after the effective date of the new rules, IXCs with annual toll revenues in excess of $100 million must contribute monthly to a fund to be paid out pro rata to PSPs; the amount each IXC must contribute is based upon its share of total long distance toll revenues. The total amount to be paid into the fund is determined by multiplying the average number of compensable calls made from payphones each month by $0.35, the price of a local call in the majority of deregulated states. For the second year of the interim period, all IXCs must pay the PSPs either a negotiated rate or the default per-call rate of $0.35 for each compensable call. *Order* ¶¶ 50-51, 72, 117-26.

In order to ensure that LECs would be unable to subsidize their payphone operations with revenues from other

telephone services, the Commission decided to treat all LEC payphones as unregulated, untariffed customer premises equipment; accordingly, the LECs must transfer their payphone assets from their regulated accounts to their unregulated accounts. *Order* ¶¶ 142-43. As a consequence the LECs have to "reduce their interstate CCL charges by an amount equal to the interstate allocation of payphone costs currently recovered through those charges." *Order* ¶ 181; *Reconsideration* ¶ 170. The Commission did not, however, require the LECs to provide payphone service through structurally separate affiliates; an LEC may instead maintain its payphone assets on its own books provided that it treats those assets as unregulated. *Order* ¶ 157. As explained below, the method for the valuation of the LEC's payphone assets depends upon whether the LEC transfers them to a separate corporate entity or merely segregates them for the purpose of regulatory accounting. *Id.* ¶ 162.

Finally, the Commission required the BOCs to make available to all PSPs without discrimination any basic services it provides to its own payphone affiliate or division. The Commission did not prohibit the BOCs from discriminating against PSPs in the provision of untariffed services, such as the installation and maintenance of equipment, billing and collection for payphone services, and the provision of operator services. *Order* ¶ 149; *Reconsideration* ¶ 166.

II. ANALYSIS

The various petitions for review now before the court challenge different aspects of the Commission's new payphone regulations. The State regulatory commissions and the National Association of the State Utility Consumer Advocates *et al.* (NASUCA) contend that the Commission lacks authority to regulate, or in this instance to deregulate and prevent the States from regulating, rates for local coin

calls. The IXCs argue that the Commission acted arbitrarily and capriciously insofar as it (1) used the rate for local coin calls in the majority of States that have deregulated their local coin call rates as the basis for determining the interim compensation for access code and subscriber 800 calls; (2) excused IXCs with toll revenues of less than $100 million from compensating PSPs for such calls during the first year of the interim compensation period; and (3) adopted the local coin call rate that a PSP sets at each payphone as the default rate of permanent compensation for access code and subscriber 800 calls made from that phone. Members of the paging industry, Personal Communications Industry Association *et al.* (PCIA), contend that the Commission arbitrarily and capriciously required carriers, rather than callers, to pay PSPs for access code and subscriber 800 calls; a group of IXCs (led by Cable & Wireless, Inc.) join PCIA's challenge to the Commission's decision to require the carriers to track such calls as well. Two IXCs (Telco Communications Group, Inc. and Excel Telecommunications, Inc.) argue that the Commission did not give the parties adequate notice that it was planning to adopt a market-based interim compensation scheme. The American Public Communications Council *et al.* (APCC) and the Regional Bell Operating Companies (RBOCs), which are the seven holding companies that own the BOCs, challenge the Commission's choice of methodologies for valuing payphone assets transferred from regulated to unregulated status; the RBOCs also contend that the Commission arbitrarily and capriciously excluded inmate and other 0+ calls from the interim compensation plan.

A. Jurisdiction over Intrastate Rates

[1] The utility regulatory commissions of nine states, as petitioners, and the NASUCA, as an intervenor, argue that the Act does not give the Commission the authority to

preempt the States' power to regulate local coin rates. The Supreme Court has held that "[t]he crucial question in any preemption analysis is always whether Congress intended that federal regulation supersede state law." *Louisiana Public Serv. Comm'n v. FCC*, 476 U.S. 355, 369, 106 S.Ct. 1890, 1898, 90 L.Ed.2d 369 (1986). In the quoted case the Court explained that in the Communications Act of 1934 the Congress set up a dual system of state and federal regulation of telephone service: under § 151 the FCC has the power to regulate "interstate and foreign commerce in wire and radio communication," but under § 152(b) we are advised that "nothing in [the Act] shall be construed to apply or give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier." 47 U.S.C. §§ 151, 152(b). The Court read § 152(b) as "not only a substantive jurisdictional limitation on the FCC's power, but also a rule of statutory construction." 476 U.S. at 373, 106 S.Ct. at 1900. Because § 276 of the Telecommunications Act of 1996 is an amendment to the 1934 Act, it too is subject to the substantive and interpretative limitations of § 152(b). Therefore, § 276 should not be read to confer upon the FCC jurisdiction over local coin rates unless § 276 is "so unambiguous or straightforward so as to override the command of § 152(b)." *Id.* at 377, 106 S.Ct. at 1902.

As we have seen, the Congress in § 276 directed the Commission to establish regulations to "ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call." The indicated petitioners and intervenors contend that § 276(b) does not manifest the clear congressional intent necessary to preempt the States' power over local coin rates. They claim that the term "compensation" is not used interchangeably in the Act with the phrase "rates and charges," which appears in § 226(b)(1)(C) (providing that OSPs are required to disclose

to their customers "a quote of its rates or charges for a call"), or with the phrase "local coin rate," a term of art with which the Congress is familiar. Their point is that if the Congress had intended to give the Commission jurisdiction over local coin rates, instead of requiring only generally that PSPs be "fairly compensated," then it would have stated specifically that it was giving the Commission the authority to set the rates for such calls.

It is undisputed that local coin calls are among the intrastate calls for which payphone operators must be "fairly compensated"; the only question is whether in § 276 the Congress gave the Commission the authority to set local coin call rates in order to achieve that goal. We conclude that it did. The States' and the NASUCA's argument to the contrary notwithstanding, the Congress has in fact used the term "compensation" elsewhere in the Act in such a way so as to encompass rates paid by callers. For example, § 226 provides that "[t]he Commission shall consider the need to prescribe compensation (other than advance payment by consumers) for owners of competitive payphones"; if the petitioners were correct, then the parenthetical exception would be mere surplusage. The Congress also has used the term "compensation" in other parts of the Act in such a way as to include payments made by customers. *See* 47 U.S.C. § 203(c)(1) (providing that a common carrier may not "charge, demand, collect, or receive a greater or less or different compensation"--i.e., from customers--than that set forth in its tariffs); 47 U.S.C. § 309(j)(2)(A) (providing that competitive bidding may be used to grant licenses to use the electromagnetic spectrum if the "principal use of such spectrum will involve, or is reasonably likely to involve, the licensee receiving compensation from subscribers."). Because the only compensation that a PSP receives for a local call (aside from the subsidies from CCL charges that LEC payphone providers enjoy) is in the form of coins deposited into the phone by the caller, and there is no

indication that the Congress intended to exclude local coin rates from the term "compensation" in § 276, we hold that the statute unambiguously grants the Commission authority to regulate the rates for local coin calls.

[2] The States and the NASUCA next argue that even if the Commission has jurisdiction over local coin rates, its decision to deregulate those rates was arbitrary and capricious because the Commission did not adequately take into account the possibility of "locational monopolies" with substantial market power. Here the States and the NASUCA have in mind situations in which a PSP obtains an exclusive contract for the provision of all payphones at an isolated location, such as an airport, stadium, or mall, and is thereby able to charge an inflated rate for local calls made from that location. *See Order* ¶ 59.

The Commission did not ignore the possibility of problematic locational monopolies, however; rather it concluded that it would deal with them if and when specific PSPs are shown to have substantial market power. *Order* ¶ 61; *Reconsideration* ¶ 62. The petitioners and intervenors failed to present any evidence that there are significant locational monopolies in the states that have already deregulated their local coin rates; accordingly, it was not unreasonable for the Commission to conclude that market forces generally will keep prices at a reasonable level, thereby making locational monopolies the exception rather than the rule. If locational monopolies turn out to be a problem, however, the Commission suggested some ways in which it might deal with them: a State might be permitted to require competitive bidding for locational contracts, or to mandate that additional PSPs be allowed to provide payphones at the location; and if these remedies fail, the Commission may consider the matter further. *Order* ¶ 61. Indeed, the Commission specifically reserved the right to modify its deregulation scheme, for example, by limiting the number of compensable calls from each payphone. *Id.*

[3] The NASUCA argues that the Commission's authority to act under § 276 must be narrowly tailored in order to avoid unnecessarily preempting the States' power to act. In this vein it contends that the Commission did not have to preempt the States' authority to regulate local coin rates in order to promote the widespread deployment of payphone services. The FCC points out that its regulation of intrastate matters must be as narrow as possible only when the preemption arises by implication--for example, where it is impossible to regulate interstate matters without regulating intrastate matters. *See Public Serv. Comm'n of Maryland v. FCC*, 909 F.2d 1510, 1514-15 (D.C.Cir.1990); *Public Utility Comm'n of Texas v. FCC*, 886 F.2d 1325, 1331-32 (D.C.Cir.1989). In this case the Commission has never argued that it has jurisdiction over local coin call rates merely by implication. Rather, as we have seen, the Commission has been given an express mandate to preempt State regulation of local coin calls. Accordingly, the requirement that the FCC's regulation be narrowly tailored simply does not come into play.

[4] Finally, the petitioners argue that if the Commission has the authority to regulate the rates for local coin calls, then it may not forebear from regulating them—that is, by relying upon market forces to determine prices—unless it makes the three findings required by 47 U.S.C. § 160. These are that enforcement of the Act or regulation is not necessary (1) to ensure "just and reasonable" nondiscriminatory charges, or (2) "for the protection of consumers," and that (3) forbearance is "consistent with the public interest." The Commission responds that it did not forbear from applying any regulation or any provision of the Act, as contemplated by § 160, because it did establish a compensation plan in accordance with the directive of the statute. We agree. A market-based approach is as much a compensation scheme as a rate-setting approach; hence § 160 is simply not relevant to the regulations presently under review.

B. Setting Compensation for 800 and Access Code Calls Equal to the Deregulated Local Coin Rate

[5] The FCC decided that the compensation rate for 800 and access code calls should be equal to the deregulated local coin rate. The FCC rested this conclusion on one ground--that the costs of coin calls, 800 calls, and access code calls all are similar:

> If a rate is compensatory for local coin calls, then it is an appropriate compensation amount for other calls as well, *because the cost[s] of originating the various types of payphone calls are similar.*

Order ¶ 70 (emphasis added); *see also id.* ("[W]e conclude that deregulated local coin rates are the best available surrogates for payphone costs...." (emphasis added)); *Reconsideration* ¶ 71 ("[T]he costs of originating the various types of payphone calls are similar."). No other justification was offered by the FCC for its conclusion.

The problem with the FCC's decision is that the record in this case is replete with evidence that the costs of local coin calls versus 800 and access code calls are *not* similar. Numerous IXCs pointed out that the costs of coin calls are higher than those for coinless calls because of the costs typically associated with use of coin equipment (*e.g.*, the costs of purchasing the equipment and coin collection). *See, e.g.*, AT&T Reply 6 (July 15, 1996); Cable & Wireless, Inc., Petition for Reconsideration 5-6 (Oct. 21, 1996); Comments of Sprint Corporation 9 (July 1, 1996); WorldCom, Inc., Petition for Reconsideration 8-9 (Oct. 21, 1996). In addition, IXCs showed that costs of local coin calls are higher because the PSP bears the costs of originating and completing local calls (*i.e.*, the "end-to-end" costs); by contrast, for coinless calls, the PSP only bears the costs of originating the calls. *See, e.g.*, AT&T Reply 12-13; Comments of Sprint

Corporation 9. Even the APCC, a trade group for independent PSPs, acknowledged that the costs of coin calls are higher than those of coinless calls. *See* Comments of the American Public Communications Council 16 n.15 (July 1, 1996) ("Arguably the local coin rate should be *higher* than the rate for a [coinless] call because of the usage and coin collection costs typically associated with local coin calling."). AT&T estimated that the costs of local coin calls are three times higher than those of coinless calls. *See* AT&T Reply 8-9.

The FCC failed to respond to any of the data showing that the costs of different types of payphone calls are not similar. Rather, the FCC's *Order* cavalierly proclaims that the costs of local coin calls versus 800 and access code calls are "similar," *without even acknowledging any of the contrary data. See Order* ¶ 70. The agency's order on *Reconsideration* at least recognizes that some parties had argued that the costs of coin calls are not "similar" to those of 800 and access code calls; but the FCC then dismissed the argument with two words—"We disagree"—and never provided any reasons for its "disagreement." *See Reconsideration* ¶ 71. The FCC's *ipse dixit* conclusion, coupled with its failure to respond to contrary arguments resting on solid data, epitomizes arbitrary and capricious decisionmaking. *See Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29, 46-57, 103 S.Ct. 2856, 2868- 73, 77 L.Ed.2d 443 (1983).

The FCC contends that even if the compensation rate is unsupported, it should be upheld because it is only a "default" rate. In other words, the FCC claims that IXCs will be able to "block" calls from overpriced payphones and, therefore, will be able to negotiate lower rates if the local coin rates are too high. *See Reconsideration* ¶ 71. This possibility, however, does not save a default rate that is inexplicably tied to a local coin rate.

We have no good reason to doubt the FCC's conclusion that the IXCs' potential to block calls gives them some

leverage to negotiate. Although the IXCs protest that they cannot *currently* recognize overpriced payphones in "real time," *see* AT&T Reply 4 n.8, they do not argue that they lack the technology to do so. In fact, at oral argument, counsel for the IXCs all but conceded that the relevant technology is currently available. *See* Tr. of Oral Argument at 15-19. We therefore conclude that the FCC's assumption that IXCs have the capacity to "block" calls is reasonable. *See Telocator Network of Am. v. FCC*, 691 F.2d 525, 539-42 (D.C.Cir.1982). However, this conclusion does not save the default compensation rate for 800 and access code calls. The critical point here is that the FCC has failed to justify tying the default rate to local coin rates; and the mere possibility that the default rate *might* be adjusted by negotiation does not negate the fact that it is arbitrary. Indeed, blocking is hardly an ideal option for the IXCs, for it is not only expensive to implement, *see, e.g.*, Petition of Sprint for Reconsideration 10 n.8 (Oct. 21, 1996); Tr. of Oral Argument at 19 (counsel for the IXCs, without contradiction, stated that blocking is "immensely more expensive" then tracking), but its use invariably will result in a mutual loss of business for *both* the PSPs and the IXCs. Thus, at a minimum, the IXCs are entitled to a default rate that is reasonably justified, so they are not forced to resort to blocking only because the default rate has been set at an unreasonable level.

In short, the FCC's conclusion that compensation for 800 and access code calls should be set at the deregulated local coin rate is unjustified. Accordingly, we remand this issue to the agency for further consideration.

C. Interim Plan

1. Compensation for 800 and Access Code Calls During the Interim Period

[6] The IXCs also challenge the FCC's interim plan for compensation for 800 and access code calls based on a rate of $.35 per call. Under the first phase of the interim plan, large IXCs (with toll revenues over $100 million) are required to pay a flat-rate compensation of $45.85 per payphone per month ($.35 per call multiplied by 131, the average number of 800 and access code calls per payphone per month); the large IXCs must pay the flat-rate compensation in proportion to their total long distance revenues. During the second phase, all IXCs are required to pay $.35 per 800 or access code call. We find that the interim plan is arbitrary and capricious for two reasons.

First, the FCC cites no reasonable justification for an interim rate based on $.35 per call. The FCC picked the $.35 figure because the $.35 rate was deemed the best approximation of a deregulated coin rate, as it is "the rate in the majority of states that have allowed the market to determine the appropriate local coin rate," *Order* ¶ 72. However, as we have already found, the FCC's decision to set compensation for 800 and access code calls at the deregulated local coin rate was arbitrary and capricious. Thus, the $.35 rate, which is an attempt to approximate the deregulated coin rate, cannot stand. The FCC must now set a new interim rate and decide what is to happen once the interim period is over. The agency may of course elect to use the new interim rate as a "default rate" at the conclusion of the interim period. If this were done, the PSPs and IXCs still could be left free to depart from the default rate through negotiations (with IXCs having to resort to blocking to gain leverage in any such negotiations).

Second, we also find that the FCC acted arbitrarily and capriciously in requiring payments only from large IXCs—those with over $100 million in toll revenues—for the first phase of the interim plan. The FCC based this decision on concerns of administrative convenience. *See Reconsideration* ¶ 126. It is far from clear that the administrative burdens are

as heavy as the FCC seems to believe them to be, as each carrier would merely be required to write a check based on its percentage of annual toll revenues. Yet, even assuming, *arguendo*, that the FCC's limitation marginally increases administrative convenience, this limitation comes at a huge cost. For example, if small IXCs were included, they could be required to pay as much as $4 million *per month*. As the small IXCs concede, this amount is "far from *de minimis*." Final Brief of Intervenor Telecommunications Resellers Association at 9. Administrative convenience cannot possibly justify an interim plan that exempts all but large IXCs from paying for the costs of services received. Perhaps more fundamentally, the FCC did not adequately justify why it based its interim plan on total toll revenues, as it did not establish a nexus between total toll revenues and the number of payphone-originated calls. Accordingly, we grant the petition for review on these points, and remand the matter to the FCC for further consideration.

2. Compensation for 0+ Calls During the Interim Period

[7] Section 276 requires the Commission to "prescribe regulations that establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone." 47 U.S.C. § 276(b)(1)(A). The Commission's *Order*, however, limits compensation during the first interim year to access code and 800-calls. *Order* ¶ 124-25. PSPs will therefore receive no interim compensation for so-called "0+" calls. Nowhere does the Commission explain why this is so.

[8] The RBOCs complain that the Commission's failure to provide compensation for 0+ calls is both unreasoned and contrary to the plain language of § 276. The Commission does not dispute this claim on the merits. It argues rather that we should not consider the RBOCs' claim because they

failed to raise it before the Commission. 47 U.S.C. § 405. We disagree.

The RBOCs mentioned the argument in their petition for clarification, but stated that they did not "anticipate any challenge to the Commission's failure to include, in its interim compensation levels, an estimate of the 0+ calls carried by RBOC payphones." RBOC Petition for Clarification at 5 n.1. The Commission uses this language to argue that the RBOCs affirmatively abandoned this claim in their proceedings before the Commission and cannot therefore raise it in this court. The Commission, however, focuses only on a single sentence. The next sentence reads, "[s]o long as the interim compensation mechanism provides *some level* of recompense ... on 0+ calls where RBOCs are not otherwise compensated, the RBOCs see no reason to upset the Commission's balance of competing concerns." *Id.* (emphasis in original). The RBOCs' promise to refrain from challenging this portion of the regulations was conditioned on the Commission's provision of "some level of recompense" for 0+ calls during the first interim year. The Commission's final interim plan included no such "level of recompense." The RBOCs did not, therefore, abandon this claim. Their petition for clarification gave the Commission an "opportunity to pass" upon this question. That is all that § 405 requires. We therefore reject the Commission's waiver argument. On the merits, it is clear that the RBOCs are correct. The Commission's failure to provide interim compensation for 0+ calls is patently inconsistent with § 276's command that fair compensation be provided for "each and every completed ... call." The Commission's failure to provide an explanation for this seemingly illogical decision is arbitrary and capricious. On remand, the Commission must correct this flaw in the interim compensation scheme.

3. Compensation for Inmate Calls During the Interim Period

The RBOCs raise a different but related issue regarding compensation during the interim period for calls made from inmate payphones. The Commission decided that inmate payphones would not be eligible for any interim flat-rate compensation for coinless calls. The Commission said this decision was justified "because such payphones are not capable of originating either access code or subscriber 800 calls, and the interim compensation is provided only for those two types of calls." *Reconsideration* ¶ 52. The RBOCs claim that the Commission never adequately reconciled this determination with the "each and every completed call" language of § 276.

The Commission does not respond to this claim on the merits. It requests instead that we delay deciding this issue until we consider a different petition for review that also raises issues related to inmate payphones. We deny the Commission's request. There is no reason why we should defer judgment. The Commission has pointed to no way in which this issue is inextricably intertwined with the issues that we will decide in the subsequent inmate payphone case. It is entirely appropriate for us to decide this question at this time.

Doing so, we hold that the issue must be remanded to the Commission. Section 276 requires the Commission to promulgate regulations that will ensure that PSPs receive fair compensation "for each and every completed intrastate and interstate call using their payphone." 47 U.S.C. § 276(b)(1)(A). Under the regulations the Commission has promulgated, PSPs will receive no compensation for coinless calls made from inmate phones during the first interim year. This appears to be blatantly inconsistent with the language of the statute. The Commission has not explained why it is not. The Commission's interim compensation plan must therefore be remanded.

D. Carrier Pays

[9] The PCIA petitioners challenge as arbitrary and capricious the Commission's decision to adopt a "carrier pays" compensation system for 800 calls. In developing a payphone compensation system, the Commission's expressed desire was to create "a competitive payphone industry," *Order* ¶ 8, that would be both "cost effective" and "place[ ] the payment obligation on the primary economic beneficiary," *id.* ¶ 83 The Commission concluded that "carrier pays" compensation furthers each of these goals. Petitioners disagree.

Petitioners first argue that a "carrier pays" system does not—indeed, cannot—promote competition. This is so, petitioners explain, because the party causing the cost (the caller) does not have to pay it, and the party incurring the cost (the carrier, or, if the cost is passed on, the 800 service subscriber) has no way to decline it. The Commission, however, concluded that the party incurring the cost could avoid it. As the Commission explained, carriers have some leverage "to negotiate for lower per-call compensation amounts" in that they can block calls from particular payphones charging excessive rates. *Reconsideration* ¶ 66, ¶ 71. Subscribers to an 800 service can utilize a carrier's call-blocking capability by negotiating with the carrier to block calls from payphones with excessive per-call compensation charges. *Order* ¶ 17. Further, as discussed above, we have determined that the Commission reasonably concluded that carriers can and will develop blocking technology. Thus, a "buyer" (the carrier or the 800 service subscriber) will have the option of rejecting a "seller's" (the PSP) excessively priced service. Given this explanation, the Commission's conclusion that a "carrier pays" compensation system will result in competitive market pricing of 800 service payphone per-call compensation charges was not arbitrary or capricious.

Petitioners also argue that the substantial burdens of the "caller pays" system outweigh the minor inconvenience to callers of requiring coin deposits. The Commission did not disagree that the burden of requiring coin deposits was slight. *See Order* ¶ 85. Nevertheless, the Commission elected to adopt a "carrier pays" system in order to maintain the convenience of coinless calling upon which the public has come to rely. *Id.* The Commission's balancing of the competing concerns of administrative efficiency and consumer convenience was not arbitrary.

Finally, petitioners contend that the Commission's "primary economic beneficiary" analysis is flawed. The Commission concluded that the carrier is the "primary economic beneficiary" of an 800 call because the call utilizes a particular carrier regardless of where the call is originated. *Reconsideration* ¶ 88. In addition, the Commission concluded that the called party received "greater economic benefit" from an 800 service call than the calling party as evidenced by the fact that the called party is willing to pay for the call. *See id.* As a result, the Commission concluded that it was appropriate for carriers to bear the per-call compensation charges for the calls, and that "the IXC can best pass on ... any charges for compensable calls" to the 800 service subscribers. *Id.* Petitioners argue that this analysis is arbitrary in that a carrier benefits from an 800 service call regardless of whether that call is made from a payphone or a home phone. It is the caller that primarily benefits from the use of the payphone. We fail to understand petitioners' point. The Commission did not disagree with petitioners that carriers (and subscribers) benefit from 800 service calls regardless of the source of the call. *See id.* What the Commission concluded was that as the "primary economic beneficiaries" of 800 service calls, carriers should incur the costs of the calls which, in the case of payphone calls, now include per-call compensation charges. The Commission's judgment on this matter was neither arbitrary nor capricious.

We therefore reject petitioners' challenge to the "carrier pays" compensation scheme.

E. Tracking

[10] We can quickly dispose of the argument, made by a subset of IXCs, that the FCC acted arbitrarily and capriciously in requiring that IXCs "track" payphone calls. In its *Order*, the FCC concluded that "the requisite technology exists for IXCs to track calls from payphones." *Order* ¶ 96. None of the commenters disputed this claim. Instead, the complaining IXCs merely argue that the call tracking responsibility should be placed on *another* party. The FCC, however, acted well within the bounds of reasonableness in assigning this responsibility to the IXCs. As a result, we deny the petition for review on this claim.

F. Non-discrimination

[11] The APCC petitioners challenge the Commission's decision to prohibit discrimination by BOCs only in the provision of basic services. According to petitioners, the nondiscrimination mandate of § 276(a)(2) of the Communications Act requires that the Commission adopt regulations prohibiting all discrimination by BOCs, including discrimination in the provision of basic services. We, of course, review an agency's construction of a statute which it administers under the two-step test developed by the Supreme Court in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984). Under the first step of the Chevron test, we ask "whether Congress has directly spoken to the precise question at issue." *Id.* at 842, 104 S.Ct. at 2781. If so, "that is the end of the matter." *Id.* However, if Congress has not spoken directly to the question at issue, we then ask "whether the agency's answer is based on a permissible construction of

the statute." *Id.* at 843, 104 S.Ct. at 2781. We apply this test to the FCC's construction of § 276.

[12] Section 276(a)(2) of the Communications Act provides that "any Bell operating company that provides payphone service ... shall not prefer or discriminate in favor of its payphone service." 47 U.S.C. § 276(a)(2). This command, taken alone, appears to express an unambiguous congressional intent to eliminate all discrimination by BOCs in favor of their payphone services. However, under step one of *Chevron*, we consider not only the language of the particular statutory provision under scrutiny, but also the structure and context of the statutory scheme of which it is a part. *Amalgamated Transit Union v. Skinner*, 894 F.2d 1362, 1368 (D.C.Cir.1990). Considering these other indicators of congressional intent, the command of § 276(a) is far from clear.

Subsection (b) of § 27 requires the Commission to adopt "regulations that ... prescribe a set of nonstructural safeguards ... to implement the provisions of ... subsection (a), which safeguards shall, at a minimum, include the nonstructural safeguards equal to those adopted in the *Computer Inquiry—III* ... proceeding." *Id.* § 276(b)(1)(C). The safeguards adopted in the *Computer Inquiry—III* proceeding do not prohibit all discrimination in the provision of nontariffed services to independent PSPs. *See In the Matter of Computer III Remand Proceedings: Bell Operating Company Safeguards and Tier 1 Local Exchange Company Safeguards*, 6 F.C.C.R. 7571, 7575-76 (1991). Section 276(b)(1) thus implies that Congress did not view the elimination of discrimination in the provision of nontariffed services as necessary to comply with the command of § 276(a). Although petitioners point us to a House Report concerning § 276 which expresses an intent to " 'eliminate *all* discrimination between BOC and independent payphones,' " H.R.REP. NO. 104-204(I), at 88 (1995) (emphasis added), the language and structure of the statute

enacted do not establish an unambiguous congressional intent to eliminate all discrimination in the provision of nontariffed services.

We therefore proceed to step two of the *Chevron* test and ask whether the Commission's resolution of the ambiguity in § 276 was "permissible." The Commission concluded that it was unnecessary to prohibit BOC discrimination in the provision of nontariffed services as those services "are available on a competitive basis and do not have to be provided by [BOCs] as the only source of services." *Reconsideration* ¶ 166. This policy judgment is both reasonable and consistent with the Act's purposes of "promot[ing] competition and reduc [ing] regulation." Pub.L. No. 104-104. We therefore hold that the Commission's interpretation of § 276 as only requiring regulations eliminating discrimination in the provision of basic services was permissible.

G. Payphone Asset Valuation

[13] Finally, both the BOC and APCC petitioners challenge as arbitrary the Commission's method of valuing payphone assets. Section 276(a)(1) provides that "any Bell operating company that provides payphone service shall not subsidize its payphone service directly or indirectly from its telephone exchange service operations or its exchange access operations." *Id.* U.S.C. § 276(a)(1). Subsection (b) of § 276 requires the Commission to issue "regulations that ... discontinue ... all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues." 47 U.S.C. § 276(b)(1)(B). The Commission's rules governing the accounting valuation of assets transferred between affiliates ("affiliate transaction rules") provide that:

> Assets sold or transferred between a carrier and its affiliate pursuant to a tariff, including a tariff filed with a state commission, shall be

> recorded in the appropriate revenue accounts at the tariffed rate. Non-tariffed assets sold or transferred between a carrier and its affiliate that qualify for prevailing price valuation, as defined in paragraph (d) of this section, shall be recorded at the prevailing price. For all other assets sold by or transferred from a carrier to its affiliate, the assets shall be recorded at the higher of fair market value and net book cost.

47 C.F.R. § 32.27(b).

Interpreting these provisions, the Commission concluded that an LEC providing payphone service may, but need not transfer its payphone operations to a "structurally separate affiliate[ ]." *See Order* ¶ 157. Those LECs that elect not to transfer their payphone assets to a separate affiliate may maintain the assets on the books at net book value. *Id.* ¶ 163. If, on the other hand, an LEC transfers its "payphone assets to either a separate affiliate or an operating division that has no joint and common use of assets or resources with the LEC and maintains a separate set of books," the LEC must record the transfer of assets at the higher of fair market value or net book value. *Id.* ¶ 164. Fair market value includes the value of "intangible assets such as location contracts." *Id.* According to the Commission, fair market valuation will "effectively capture[ ] on the carrier's books any appreciation in value of those assets, thus ensuring that any eventual gains would accrue to the benefit of the ratepayers and shareholders." *Id.* ¶ 166. The BOC petitioners contend that the Commission acted arbitrarily in requiring fair market valuation of those payphone assets transferred to a separate affiliate or operating division. Conversely, the APCC petitioners argue that the Commission acted arbitrarily in requiring the use of net book value for payphone assets not transferred.

As a general rule, utility service ratepayers "pay for

service" and thus "do not acquire any interest, legal or equitable, in the property ... of the company. Property paid for out of moneys received for service belongs to the company." *Board of Pub. Util. Comm'rs v. New York Tel. Co.*, 271 U.S. 23, 32, 46 S.Ct. 363, 366, 70 L.Ed. 808 (1926). However, we have held that neither ratepayers nor the company (and thus its shareholders) are necessarily entitled to increases in the value of assets employed in the utility's operations. *See Democratic Cent. Comm. of the Dist. of Columbia v. Washington Metro. Area Transit Comm'n*, 485 F.2d 786, 805 (D.C.Cir.1973), *cert. denied*, 415 U.S. 935, 94 S.Ct. 1451, 39 L.Ed.2d 493 (1974). Rather, such increases are to be allocated under a two-step test in which the court first asks which party "bears the risk of loss" on the assets. *AT&T Info. Sys., Inc. v. FCC*, 854 F.2d 1442, 1444 (D.C.Cir.1988). The party that bore the risk of loss is the party entitled to the capital gains on the assets. *See id.* Only if it is difficult to determine who bore the risk of loss will "the second principle come[ ] into play, namely, 'that those who bear the financial burden of particular utility activity should also reap the benefits resulting therefrom.' " *Id.* (quoting *Democratic Cent.*, 485 F.2d at 808).

In developing its valuation methodology, the Commission declined to apply the two-step test we developed in *Democratic Central*. According to the Commission, that test is not "directly applicable either to the situation where a carrier retains the payphone assets on its books or transfers the payphone assets to a separate affiliate." *Order* ¶ 168. Instead, the Commission concluded that its affiliate transaction rules adequately protected the interests of ratepayers. *Id.* Taken alone, this conclusion may be correct. But the Commission fails to recognize that our test in *Democratic Central* was designed to protect not only the interests of ratepayers, but also the competing interests of shareholders. *See* 485 F.2d at 806. By adopting a going concern valuation methodology, the Commission was

attempting to transfer the increase in the value of the payphone operations from the LECs (and their shareholders) to ratepayers. This was plainly inappropriate under *Democratic Central*.

As explained above, in allocating increases in asset value under *Democratic Central*, we first ask which party bore the risk of loss on the assets. The answer to that question may change over time depending on the regulatory scheme in place. Prior to October 1990, the FCC regulated the rates of local telephone exchange companies under a rate-of-return regulatory system. *See Policy and Rules Concerning Rates for Proposed Dominant Carriers, Further Notice of Proposed Rulemaking*, 3 F.C.C.R. 3195 (1988). Under a rate-of-return system, a company "can charge rates no higher than necessary to obtain sufficient revenue to cover" the costs of regulated activities and "achieve a fair return on equity." *See National Rural Telecom Ass'n v. FCC*, 988 F.2d 174, 177-78 (D.C.Cir.1993) (internal quotations and citations omitted). The provision of payphone service traditionally has been treated as a regulated activity. *See* 47 C.F.R. §§ 32.2351, 32.6351, 32.5010. Thus, LEC shareholders were protected against losses from depreciation expenses on the assets of regulated activities; it was ratepayers who bore the risk of loss on such assets. *See AT&T Info. Sys.*, 854 F.2d at 1444.

However, in October 1990, the Commission switched to a "price cap" system of regulating the larger LECs (*i.e.*, the BOCs and GTE companies). *Policy and Rules Concerning Rates for Dominant Carriers: Second Report and Order*, 5 F.C.C.R. 6786 (1990). Under a price cap system, "the regulator sets a maximum price, and the firm selects rates at or below the cap." *National Rural Telecom*, 988 F.2d at 178. Cost reductions under the price cap scheme "do not trigger reductions in the cap," but rather increase the company's profits. *See id.* Thus, after 1990, the ratepayers no longer bore the risk of losses from payphone operation assets. To

the extent a BOC incurred expenses in connection with payphone operations, company and shareholder profits declined. As a result, at least since 1990, investors rather than ratepayers have borne the risk of loss on payphone assets (tangible and intangible), and thus, under *Democratic Central*, investors should reap the benefit of increases in the value of such assets.

The Commission argues that our decision in *Southwestern Bell Corp. v. FCC*, 896 F.2d 1378 (D.C.Cir.1990), forecloses the BOCs' challenge to the Commission's interpretation and application of the affiliate transaction rules to this case. We disagree. In *Southwestern Bell*, we upheld the Commission's affiliate transaction rules against a challenge by the GTE companies. In so doing, we specifically rejected the argument that the Commission's affiliate transaction rules violated *Democratic Central*. *Id.* at 1381. We concluded that a deviation from the rule of *Democratic Central* was appropriate in the case of "complex, ongoing affiliate transactions" so that the Commission could guard against systematic cost misallocation by the local exchange companies. *Id.* at 1381-82. However, we specifically noted *Democratic Central's* continued applicability to "one- time" transfers mandated by industry reform. *Id.* at 1382. In this case, the Commission's affiliate transaction rules as applied to the transfer of payphone assets pursuant to § 276's command to discontinue payphone subsidies clearly falls within the latter category of transactions. Thus, the BOCs' challenge to the Commission's application of its rules was not foreclosed by *Southwestern Bell*.

The APCC petitioners argue that the Commission erred in allowing payphone assets to be placed in regulated accounts at net book value rather than fair market value. We reject the APCC petitioners' challenge to the net book valuation method for the same reasons we accept the BOCs' challenge to the Commission's fair market method. The risk of loss on payphone assets was borne by shareholders. Thus, any

increases in the value of the payphone operations belongs to the shareholders, not the ratepayers. *Democratic Central*, 485 F.2d at 806.

14] We also reject the APCC petitioners' argument that § 276 requires that a BOC's payphone assets be transferred to its unregulated books. Section 276 simply requires that payphone subsidies be discontinued. 47 U.S.C. § 276(b)(1)(B). The Commission interpreted this provision as requiring only that payphone assets not transferred to a separate affiliate be accounted for under the *Computer Inquiry—III* nonstructural safeguards. *Order* ¶ 157. These safeguards were designed to "effectively protect against cross-subsidization." 6 F.C.C.R. at 7575. We fail to see how the application of these safeguards to payphone service operations violates § 276's command to discontinue payphone subsidies.

In sum, we agree with the BOC petitioners that the Commission's fair market valuation methodology is arbitrary and capricious and contrary to our precedent. Therefore, we will vacate and remand that portion of the Commission's order for further proceedings. However, we reject the APCC petitioners' argument that the Commission's net book valuation method is arbitrary or contrary to the command of § 276.

III. CONCLUSION

For the foregoing reasons, we grant in part and deny in part the petitions for review.

So ordered.

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

SEPTEMBER TERM, 1997
NO. 96-1394

ENTERED: September 16, 1997

Illinois Public Telecommunication Association,
Petitioner,

v.

Federal Communications Commission and United States of America,
Respondents.

Competitive Telecommunications Association, et. al.
Intervenors.

Consolidated with 96-1395, 96-1407, 96-1428, 96-1429, 96-1466, 96-1476, 96-1478, 96-1479, 96-1482, 96-1484, 96-1485, 97-1016, 97-1021, 97-1022, 97-1039, 97-1048, 97-1069, 97-1070, 97-1080

Before: Edwards, Chief Judge, Ginsburg and Sentelle, Circuit Judges

ORDER

Upon consideration of the petitions for rehearing of The Virginia State Corporation Commission and of the Consumer Intervenors, it is

ORDERED that the petitions be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk
/s/
By: Robert A. Bonner
Deputy Clerk

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

September Term, 1997
No. 96-1394

ENTERED: September 16, 1997

Illinois Public Telecommunications Association,
Petitioner,

v.

Federal Communications Commission and United States of America,
Respondents.

Competitive Telecommunications Association, et. al.,
Intervenors.

Consolidated with 96-1395, 96-1407, 96-1428, 96-1429, 96-1466, 96-1476, 96-1478, 96-1479, 96-1482, 96-1484, 96-1485, 96-1486, 97-1016, 97-1021, 97-1022, 97-1039, 97-1048, 97-1069, 97-1070, 97-1080

BEFORE: Edwards, Chief Judge; Wald, Silberman, Williams, Ginsburg, Sentelle, Henderson, Randolph, Rogers, Tatel and Garland, Circuit Judges

ORDER

Upon consideration of the Suggestions for Rehearing In Banc of the Virginia State Corporation Commission and of the Consumer Intervenors, and the absence of a request by any member of the court for a vote, it is

ORDERED that the suggestions be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Robert A. Bonner
Deputy Clerk

Circuit Judges Wald, Henderson and Garland did not participate in this matter.

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

SEPTEMBER TERM, 1997
NO. 96-1394

ENTERED: October 7, 1997.

Illinois Public Telecommunications Association,
Petitioner,

v.

Federal Communications Commission and United States of America,
Respondents.

Competitive Telecommunications Association, et. al.,
Intervenors.

Consolidated with 96-1395, 96-1407, 96-1428, 96-1429, 96-1466, 96-1476, 96-1478, 96-1479, 96-1482, 96-1484, 96-1485, 96-1486, 97-1016, 97-1021, 97-1022, 97-1039, 97-1048, 97-1069, 97-1070, 97-1080

BEFORE: Edwards, Chief Judge, Ginsburg and Sentelle, Circuit Judges

ORDER

Upon consideration of the petition for rehearing of Intervenor APCC filed on September 23, 1997, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Robert A. Bonner
Deputy Clerk

UNITED STATES COURT OF APPEALS
FO THE DISTRICT OF COLUMBIA CIRCUIT

SEPTEMBER TERM, 1997
NO. 96-1394

ENTERED: October 7, 1997.

Illinois Public Telecommunications Association,
Petitioner,

v.

Federal Communications Commission and United States of America,
Respondents.

Competitive Telecommunications Association, et. al.,
Intervenors.

Consolidated with 96-1395, 96-1407, 96-1428, 96-1429, 96-1466, 96-1476, 96-1478, 96-1482, 96-1484, 96-1485, 96-1486, 97-1016, 97-1021, 97-1022, 97-1039, 97-1048, 97-1069, 97-1070, 97-1080

BEFORE: Edwards, Chief Judge, Wald, Silberman, Williams, Ginsburg, Sentelle, Henderson, Randolph, Rogers, Tatel and Garland, Circuit Judges

ORDER

Upon consideration of Intervenor's (APCC) Suggestion for Rehearing In Banc, and the absence of a request by any member of the court for a vote, it is

ORDERED that the suggestion be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/
Robert A. Bonner
Deputy Clerk

Circuit Court Judges Wald, Henderson, and Garland did not participate in this matter.

In the Matter of	)	
	)	
UNIVERSAL PAYPHONE CORP.	)	FCC 85-222
	)	50 FR
Petition for Declaratory Ruling	)	

58 R R 2d

Adopted: April 26, 1985
Released: May 6, 1985

MEMORANDUM OPINION AND ORDER

* * * * *

DISCUSSION

15. We observe initially that the intrastate and local exchange services used in conjunction with instrument implemented coin telephones are regulated by state authorities. When an entity subscribes to such services, and attaches a coin instrument to them and makes it available for use by others, this use of the services inherently involves resale thereof. Regulation of such resale of intrastate and local exchange services has heretofore been left to state authorities. Moreover, the terms and conditions under which intrastate pay telephone offerings are made to the public involve questions of an essentially local nature. In our Registration of Coin Operated Telephone decision, we determined that while it was appropriate to register instrument implemented coin telephones, and that the telephone companies must permit their interconnection, the use of the services with which they would be interconnected would remain subject to conditions in applicable tariffs, state or federal. Since interstate MTS and WATS tariffs authorize resale, the telephone may be used for instrument

implemented interstate pay service. Their use for intrastate and local exchange pay service, however, would be subject to any applicable resale regulations in the tariffs of such services. Thus, this decision did not alter the traditional regulatory framework where state authorities regulate intrastate and local pay telephone services. As the Commission stated in Registration of Coin Operated Telephones, supra, "states may continue to determine the conditions under which these instruments may be used for local or intrastate toll services." 49 FR at 27766, n. 24.

16. Turning to the particular state actions before us, it appears that the MPSC has determined that under applicable local statutes a person offering intrastate communications service to the public, including pay telephone service, is a public utility requiring state certification. The determination that an entity offering purely local or intrastate communications on a resale basis is a utility does not violate any Commission decision.[7/] Similarly, the rates and rate structures highlighted by petitioner apply only to jurisdictionally intrastate communications. Accordingly, these intrastate rates and rate structures do not infringe or substantially impact the customer's right to interconnect COCTs to the interstate network.

Universal Payphone Corp., Memorandum Opinion and Order, 58 Rad. Reg.2d (P&F) 76, 80 (1988)

7/ Indeed, although we have foreborne from active regulation of resellers of interstate service, under our own statute such offerings have been treated as common carriage. However the Commission has previously determined that prior state certification requirements for interconnection of terminal equipment -- as opposed to the use thereof that is regulated here -- is unlawful. Commercial Communications, Inc., 81 FCC 2d 106 (1980); see also, Telerent Leasing Corp., 45 FCC 2d 204, 225 (1974).

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of

Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996

CC Docket No. 96-128

NOTICE OF PROPOSED RULEMAKING

Adopted: June 4, 1996
Released: June 6, 1996

Comments Due: June 27, 1996
Replies Due: July 8, 1996

By the Commission: Chairman Hundt issuing a statement.

Table of Contents

Topic	Paragraph No.
I. Introduction	1
II. Background	2
III. Issues	14
A. Compensation for Each and Every Completed Intrastate and Interstate Call Originated by Payphones	14
1. The Act	14
2. Discussion	15
a. Scope of Payphone Calls Covered by this Rulemaking	15

b. Entities Required to Pay Compensation 24
c. Ability of Carriers to Track Calls from Payphones 29
d. Administration of Per-Call Compensation 32
e. Per-Call Compensation Amount 35
B. Reclassification of LEC-Owned Payphones 41
1. The Act 41
2. Discussion 42
a. Classification of LEC Payphones as CPE 42
b. Transfer of Payphone Equipment to an Unregulated Status 49
c. Termination of Access Charge Compensation and Other Subsidies 50
d. Deregulation of AT&T Payphones 55
C. Nonstructural Safeguards for BOC Provision of Payphone Service 57
1. The Act 57
2. Discussion 58
a. Background 58
b. BOC CEI Plans 60
D. Ability of BOCs to Negotiate with Location Providers on the Presubscribed InterLATA Carrier 67
1. The Act 67
2. Discussion 69
E. Ability of Payphone Service Providers to Negotiate with Location Providers on the Presubscribed IntraLATA Carrier 74
1. The Act 74
2. Discussion 75
F. Establishment of Public Interest Payphones 76
1. The Act 76
2. Discussion 77
G. Other Issues 83
1. Dialing Parity 84
2. Letterless Keypads on Payphones 85
3. Other Pending Payphone Proceedings 88

4. Comments and Ex Parte Presentations 89
5. Initial Paperwork Reduction Act Analysis 93
6. Initial Regulatory Flexibility Act Analysis 95
IV. Conclusion 103
V. Ordering Clauses 104

***

II. BACKGROUND

2. Payphone service has been regulated primarily by the states as part of the LECs' basic service. For example, states have set the rates for local payphone usage. While some of the costs of payphones owned by LECs have been recovered through charges to payphone users, other components of those costs have been recovered through intrastate and interstate rates that are unrelated to payphone usage. Like LEC payphones, AT&T payphones are classified as network equipment and, therefore, may recover their costs in a similar manner.

3. In 1980, in its Computer Inquiry II, the Commission concluded that customer premises equipment ("CPE"), such as the telephone sets used by end users, should be competitively provided and that it should not be offered as part of a carrier's regulated transmission service. The Commission determined that, if carriers bundled CPE with tariffed basic service, both a consumer's freedom of choice and marketplace competition in a developing industry would be hampered. The Commission recognized the potential for carriers to engage in anti-competitive activities. For example, carriers could potentially subsidize services facing competition with revenues from regulated, monopolistic services or shift costs from a service in a competitive industry to a service that the carrier operates as a regulated monopolist. In an effort to prevent cost misallocations, the Commission concluded that BOC provision of CPE (as well as enhanced services) should be offered through a separate

subsidiary. The Commission specifically excluded coin-operated payphones from the definition of CPE. The Commission found that, unlike other CPE, which could be "unbundled" from basic exchange service, coin-operated payphones were still integrated with the LECs' network facilities and it concluded that payphones should remain part of regulated basic communications service. The Commission later extended this determination to coinless payphones.

4. At the time of the break-up of the Bell System, payphones were regarded as a part of basic local service. The Bell System payphones were classified as exchange facilities installed by the BOCs for the provision of local service to the public. Thus, the Modification of Final Judgment ("MFJ") Court's plan of reorganization assigned all Bell System payphones to the BOCs rather than to AT&T.

5. Soon after divestiture, several manufacturers developed a "smart" payphone -- payphones with sufficient computer intelligence to perform most of the control and supervision functions previously performed by a LEC's network. Because smart payphones could be separated from local exchange service, the Commission revisited its determination to exclude all payphone service from Part 68 rules governing the connection of terminal equipment to the network. In the Coin Registration Order, the Commission reaffirmed that LEC payphones would continue to be classified as network elements rather than CPE. The Commission concluded, however, that Part 68 should apply to smart payphones and recognized the right of non-LEC providers to interconnect these payphones to the interstate public switched network. As with LEC payphones, the Commission concluded in a later proceeding that the states should retain the authority to regulate the rates and other terms of payphone interconnection. The FCC also recognized that state commissions had the authority to regulate the charges, terms, and conditions of local and intrastate payphone service.

6. Since the development of smart payphones, a number of independent or "competitive" payphone owners (referred to in previous Commission orders as "private payphone owners" or "PPOs") have begun to compete with the LECs for the provision of payphone service. Currently, there are approximately 1.5 million LEC payphones and approximately 350,000 competitively provided payphones. As a general matter, neither PPOs nor the LECs own the premises where a particular payphone is located. Instead, location providers select the payphone service provider who will provide payphone services on their premises.

7. While both PPOs and incumbent LECs receive coins as compensation for most local calls placed on their payphones, there are important differences in how PPOs and LECs are compensated. PPOs generally presubscribe their payphones to an interexchange carrier ("IXC") of their own choice. That IXC provides operator services to the payphone for collect calls and calls billed to a calling card or a third party. The PPO negotiates an agreement with the presubscribed IXC, pursuant to which the IXC pays a percentage of its revenues from the payphone to the PPO. The PPO, in turn, pays a commission to the location provider based on the revenues generated by the payphone.

8. . Pursuant to the MFJ, BOCs were required to permit location providers to select the IXC to which the payphone would be presubscribed for interstate, interLATA traffic. With this requirement, the location provider makes its own contract with an IXC to share in the interLATA revenues generated by the phone, usually through a commission arrangement for each operator-service call generated by the payphone at a particular location. Therefore, while the non-BOC LECs, like the PPOs, may receive a portion of the commissions from IXCs on interLATA operator-service calls using the presubscribed carrier, the BOCs do not receive any revenue directly from these calls. On the other hand, unlike the PPOs, all LECs, including the BOCs, receive, as a part of the carrier common

line ("CCL") charges paid by IXCs, compensation for LEC provision of the facilities necessary to deliver interexchange traffic to the IXCs. The payphone element of the CCL is charged to all interexchange customers, not just to traffic originating or terminating at a payphone, and it provides compensation to the LEC for making available the payphone through which calls are routed to the IXC.

9. To date, the Commission has focused on payphones primarily in the context of its regulation of carriers that provide operator-assisted long-distance service, known as operator service providers ("OSPs"), and in particular, its implementation of the Telephone Operator Consumer Services Improvement Act ("TOCSIA"). Because operator services prior to divestiture were provided exclusively by the Bell System at tariffed rates that were familiar to callers, there was widespread consumer dissatisfaction with the varying rates and practices of many OSPs after divestiture. The Commission responded to this dissatisfaction both through the formal complaints process and through a rulemaking proceeding. In 1990, Congress enacted TOCSIA, which required all OSPs to identify themselves to consumers and quote their rates upon request. TOCSIA also required aggregators to unblock access to other carriers and post certain disclosures on or near each telephone.

10. TOCSIA directed the Commission to determine whether PPOs should receive compensation for originating interstate calls to non-presubscribed OSPs from their payphones. The Commission concluded in the Second Report and Order that a per-call compensation mechanism was preferable because it would create greater incentives for PPOs to place their payphones in locations that generate the most traffic. The Commission concluded, however, that it was not technically feasible to implement such a mechanism at that time. Instead, the Commission adopted flat-rate compensation, in the amount of $6 per phone per month, on an interim basis. Subsequently, two IXCs, AT&T and

Sprint, certified to the Commission that they were able to pay compensation on a per-call basis and petitioned the Commission for approval to pay compensation on that basis. They argued that a per-call compensation mechanism would better serve the Commission's objective to implement a more cost-based approach to compensation for calls to non-presubscribed OSPs. The Common Carrier Bureau agreed and granted AT&T and Sprint the right to pay compensation in the amount of $.25 per call in lieu of paying per-phone compensation to PPOs. The Commission later adopted a notice of proposed rulemaking, which tentatively concluded that other large IXCs should be required to pay compensation on a per-call basis. The Common Carrier Bureau also granted waivers to two incumbent LECs, Ameritech and Southwestern Bell, that claimed the ability to track payphone calls on a per-call basis and proposed to remove payphone-related costs from their CCL charges and, instead, to impose a per-call charge on IXCs for interstate calls originated from those LECs' payphones.

11. When it adopted a compensation mechanism for interstate access code calls, the Commission concluded that, because they did not involve use of a "carrier-specific access code" and were routed directly to an end user, subscriber 800 calls were not within the class of calls for which Congress in TOCSIA directed the Commission to consider compensation. The Commission, therefore, limited compensation to interstate "access code calls." In July 1992, in response to a petition for reconsideration by the American Public Communications Council ("APCC"), the Commission affirmed its conclusion that subscriber 800 calls were not within the Commission's definition of interstate "access code calls" for which compensation should be paid.

12. In 1992, after the Commission affirmed its exclusion of subscriber 800 calls from the class of compensable access code calls, the Florida Pay Telephone Association ("FPTA") sought judicial review in the United States Court of Appeals for the District of Columbia Circuit

of this aspect of the First Report and Order and the Subscriber 800 Reconsideration Order. In its Florida Payphone decision, the Court found no reason to distinguish between the routing of access code calls and subscriber 800 calls. Therefore, it reversed and remanded the case to the Commission to "consider the need to prescribe compensation for subscriber 800 calls 'routed to providers of operator services that are other than the presubscribed provider of operator services.'" The Commission's action on the remand is pending.

13. Section 276(b)(1)(A) directs the Commission to establish a compensation mechanism to ensure "that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call" from their payphones. Section 276(b)(1)(B) mandates that the Commission "discontinue the intrastate and interstate carrier access charge payphone service elements and payments ... and all intrastate and interstate subsidies from basic exchange and exchange access revenues." In addition, Section 276(b)(1)(D) directs the Commission to consider whether BOCs should be permitted to be involved with the location provider's selection of the payphone's presubscribed carrier. Together with the other subsections of Section 276, these three provisions help to establish regulatory parity for all payphone service providers ("PSPs"), whether competitive payphone owners or incumbent LECs (both independents and BOCs).

III. ISSUES

A. COMPENSATION FOR EACH AND EVERY COMPLETED INTRASTATE AND INTERSTATE CALL ORIGINATED BY PAYPHONES

1. The 1996 Act

14. As stated above, Section 276(b)(1)(A) mandates that all payphone providers, whether independents or LECs, be "fairly compensated for each and every completed intrastate and interstate call using their payphone, except that emergency calls and telecommunications relay service calls for hearing disabled individuals shall not be subject to such compensation[.]"

2. Discussion

a. Scope of Payphone Calls Covered by this Rulemaking

15. Currently, most calls originated on payphones are within one of the following categories: (1) coin calls; (2) directory assistance calls; (3) operator service ("0+" and "0-") calls; (4) access code calls (using e.g., "10XXX" codes and "1-800" or "950" carrier access numbers); and (5) subscriber 800 calls. Each of these categories can be further subdivided between local, intraLATA toll, intrastate interLATA, interstate interLATA and international. Each type of call is a potential source of revenue for the payphone owner, whether the revenue is derived from coins deposited into the payphone, through commission payments on operator service calls, or from compensation mandated by the FCC or the states.

16. The 1996 Act requires the Commission to ensure that PSPs are fairly compensated for all calls originated by their payphones. In light of the multiple sources of revenue for payphones, we seek comment on what constitutes "fair" compensation and how we should "ensure" that each PSP receives it for calls for originated by its payphones. We tentatively conclude that our mandate under Section 276(b)(1)(A) is to ensure that PSPs are "fairly compensated" for "each and every completed intrastate and interstate call" regardless of whether the PSP currently receives compensation for the particular call originated by its

payphone. We tentatively conclude, however, that we should use this mandate to prescribe compensation only when payphone providers are not already "fairly compensated." Currently, PPOs and non-BOC LECs receive compensation, pursuant to individual contracts, from the payphone's presubscribed IXC for all "0+" calls. IXCs have long competed for this type of business. Therefore, we tentatively conclude that we need not prescribe per-call compensation for 0+ calls because competition in this area ensures "fair" compensation for PSPs. We seek comment on these tentative conclusions.

17. Although the 1996 Act directs us to prescribe compensation for all calls, Congress specifically expressed its concern in the legislative history about access code calls and subscriber 800 calls, whether the calls are intrastate or interstate in destination. We tentatively conclude that, because the 1996 Act requires us to ensure fair compensation for all calls, we must at least prescribe standards for determining fair compensation for all access code calls, subscriber 800 and other toll-free number calls, and debit card calls. The compensation we prescribe in this rulemaking will extend to all such calls, whether they are intrastate or interstate in destination. We seek comment on this tentative conclusion.

18. The 1996 Act does not expressly state that compensation should extend to international calls. We find no evidence, however, of congressional intent to leave these calls uncompensated. As discussed below, we tentatively conclude that PSPs should be compensated for their costs in originating calls from their payphones. Compensating international calls would be consistent with this approach, because the costs of originating these calls are similar to the costs of originating "each and every completed intrastate and interstate call." Therefore, despite the lack of reference to international calls in Section 276(b)(1)(A), we tentatively conclude that we should exercise our general jurisdiction under Sections 4(i) and 201(b) of the Communications Act

of 1934, as amended, to ensure that PSPs are compensated for international as well as interstate and intrastate calls originating from their payphones in the United States. We seek comment on this tentative conclusion.

19. The rate for the most common type of call, the local coin call, is set by state commissions. Typically, the rate set for local coin services provided by the incumbent LECs also applies to the PPOs. In addition, for operator services rates, the rates for intrastate coin-paid toll services from competitive payphones are frequently capped by the states at the dominant carrier rate or some increment over that rate. In many jurisdictions, incumbent LECs currently do not charge the payphone caller for "411" directory-assistance calls made from their own phones. PPOs, however, often pay a charge to the incumbent LEC for directory-assistance calls made from their competitive payphones, and are not always allowed by the state to pass those charges on to callers.

20. Section 276 of the Act requires the Commission to ensure that the payphone provider receives fair compensation for each interstate and intrastate call, including local coin sent-paid calls. Section 276 also expressly preempts state regulations that are inconsistent with our regulations. We seek comment, however, on how we should exercise our jurisdiction under Section 276. We have a range of options for ensuring fair compensation for these calls, and we seek comment on which option will ensure fair compensation for PSPs with respect to local coin sent-paid calls.

21. More specifically, one option would be to set a nationwide local coin rate for all calls originated by payphones. We seek comment on whether the Commission should take such action and request that commenters identify the specific public interest benefits they believe would result from a nationwide rate, why local rates are inadequate to ensure fair compensation, the impacts of variations among the states in the local coin sent-paid rate on PSPs and the

public, and whether those impacts are predominantly local, statewide, regional or national. Another option would be for the Commission to prescribe specific national guidelines that states would use to establish a local rate that would ensure that all PSPs are fairly compensated. We seek comment on whether the Commission should take such action and request that commenters identify specific public interest benefits they believe would result from us prescribing such guidelines, what factors such guidelines should consider, how the guidelines would ensure fair compensation for local coin calls, the impacts of variations among the states in local coin rates, and whether those impacts are predominantly local, statewide, regional or national.

22. A third option for ensuring fair compensation for PSPs would be for the states, in the first instance, to continue to set the coin rates for local payphone calls according to factors within their discretion. The Commission has long recognized the interest of the states in setting end-user rates for local calls, including rates for 411 calls. Indeed, as discussed above, the states have long had a traditional and primary role in regulating payphones. The states have a significant interest in setting local call rates paid by end users, because payphones are used by some residents as a substitute for local telephone service, in addition to being used by visitors and retail customers. However, because Section 276 of the 1996 Act requires the Commission to ensure that PSPs are fairly compensated for "each and every completed intrastate and interstate call," we seek comment on what further procedures, such as a complaint or petition process, we should establish, should we ultimately determine to defer to the states in setting payphone rates. We also seek comment on what standards we could use to adjudicate any complaints or petitions that challenge a particular rate. We further ask whether the states' setting of the rates for local coin calls subject to complaint or petition would be consistent with Section 276's mandate that the Commission ensure fair compensation for

"each and every completed intrastate and interstate call." We seek comment on whether the Commission should take such action and request that commenters identify specific public interest benefits they believe would result from having coin rates for local payphone calls set by the states. In addition, we seek comment on whether we should treat intraLATA 0+ toll calls carried by the presubscribed intraLATA carrier differently from local coin calls, or treat them like local coin calls.

23. With regard to per-call compensation for subscriber 800 calls, the Commission has previously expressed its concern about the improper use of subscriber 800 numbers to increase compensation. The Commission noted in the First Report and Order that "a payphone owner could attach an autodialer to a payphone and have it place repeated 800 calls, which are free to the caller, in order to increase the amount of compensation that the payphone owner receives." We seek comment on what rules, if any, the Commission should adopt to prevent this and other types of fraud. We also seek comment on whether the autodialer problem would extend to other types of compensable calls.

***

FEDERAL COMMUNICATIONS
COMMISSION

/s/_____
William F. Caton
Acting Secretary

Before the

FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996	CC Docket No. 96-128
Policies and Rules Concerning Operator Service Access and Pay Telephone Compensation	CC Docket No. 91-35
Petition of the Public Telephone Council to Treat Bell Operating Company Payphones as Customer Premises Equipment	
Petition of Oncor Communications Requesting Compensation for Competitive Payphone Premises Owners and Presubscribed Operator Services Providers	
Petition of the California Payphone Association to Amend and Clarify Section 68.2(a)of the Commission's Rules Amendment of Section 69.2(m) and (ee) of the Commission's Rules to Include Independent Public Payphones Within the "Public Telephone" Exemption from End User Common Line Access Charges	

REPORT AND ORDER

Adopted: September 20, 1996
Released: September 20, 1996

By the Commission:
Commissioner Chong issuing a statement.

Table of Contents

Topic	Paragraph No.
I. Introduction	1
II. Background	9
III. Issues	11
The Payphone Marketplace	11
A. Compensation for Each and Every Completed Intrastate and Interstate Call Originated by Payphones	20
1. Payphone Calls Subject to this Rulemaking and Compensation Amount	21
2. Entities Required to Pay Compensation	77
3. Ability of Carriers to Track Calls from Payphones	88
4. Administration of Per-Call Compensation	102
5. Interim Compensation Mechanism	117
B. Reclassification of LEC-Owned Payphones	127
1. Classification of LEC Payphones as CPE	129
2. Transfer of Payphone Equipment to Unregulated Status	152
3. Termination of Access Charge Compensation and Other Subsidies	173
4. Deregulation of AT&T Payphones	188
C. Nonstructural Safeguards for BOC Provision of Payphone Service	192
D. Ability of BOCs to Negotiate with	

Location Providers on the Presubscribed InterLATA Carrier 208
E. Ability of Payphone Service Providers to Negotiate with Location Providers on the Presubscribed IntraLATA Carrier 253
F. Establishment of Public Interest Payphones 264
G. Other Issues 287
1. Dialing Parity 287
2. Letterless Keypads on Payphones 294
3. Oncor Petition 299
IV. Procedural Matters 300
1. Petitions for Reconsideration 300
2. Paperwork Reduction Act Analysis 303
3. Regulatory Flexibility Act Analysis 311
V. Conclusion 363
VI. Ordering Clauses 364
Appendix A Text of Section 276
Appendix B List of Parties Filing Comments
Appendix C List of Parties Filing Replies
Appendix D Immediate Rules Adopted by This Order
Appendix E Rules Adopted by This Order
Appendix F Interim Compensation Obligations

I. INTRODUCTION

1. On June 4, 1996, the Commission adopted a Notice of Proposed Rulemaking ("Notice") to implement Section 276 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996 ("1996 Act"). In this Report and Order, the Commission adopts new rules and policies governing the payphone industry that: (1) establish a plan to ensure fair compensation for "each and every completed intrastate and interstate call using [a] payphone[;]" (2) discontinue intrastate and interstate carrier access charge payphone service elements and payments and intrastate and interstate payphone subsidies from basic

46. One Call contends that the local coin rate should be used as a surrogate for a fair per-call compensation amount. Conquest argues that the Commission should cap the per-call compensation amount at the rate for a local coin call. AT&T, MCI, and the RBOCs all oppose use of a local coin rate surrogate to achieve fair compensation for PSPs. They argue that local coin rates are kept artificially low by regulators and have no relationship to either cost or the market.

47. Some commenters contend that the Commission should adopt a per-call compensation amount that is within the range established by the 1992 Second Report and Order in the access code call compensation proceeding. NTCA argues that continued use of the $.40 per call rate adopted in the Second Report and Order would not be disruptive and would ensure fair compensation for PSPs. APCC argues that the Second Report and Order sets forth the type of market-based surrogates that are appropriate for the Commission to consider in the instant proceeding. PageNet argues that the Commission should examine the $6 per month LEC access charge compensation for payphones, as set forth in the Second Report and Order, and use this amount plus an intrastate recovery element to reach an amount that could be divided by the average number of compensable calls to equal the appropriate per-call rate. The RBOCs contend, on the other hand, that the $.40 per call amount in the Second Report and Order is out of date and should be higher. AT&T and Sprint argue that the factors used in the Second Report and Order are irrelevant for determining fair compensation, because the factors do not relate to marginal cost and concern costs that are recovered through other revenue streams.

c. Discussion

48. Defining "Fair Compensation". Section 276(b)(1)(A) directs the Commission to establish a plan "to

ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone." The 1996 Act does not prescribe a particular course to achieve these goals, other than to specify that such action shall "promote competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public[.]" To comply with this mandate, we tentatively concluded in the Notice that we must provide for compensation only when PSPs are not already "fairly compensated" for a particular type of a call using a payphone. A number of commenters contend that we must look to all of a payphone's possible revenue streams and ensure that the payphone, as a whole, is fairly compensated. We disagree. We conclude that, by ensuring that all calls are fairly compensated, including those for which the PSP currently receives no revenue, we will "promote competition" among PSPs and "promote the widespread deployment of payphone services to the benefit of the general public[.]" The marketplace will necessarily determine whether or not a particular payphone is economically viable.

49. We conclude that, once competitive market conditions exist, the most appropriate way to ensure that PSPs receive fair compensation for each call is to let the market set the price for individual calls originated on payphones. It is only in cases where the market does not or cannot function properly that the Commission needs to take affirmative steps to ensure fair compensation, such as in the following situations. First, because TOCSIA requires all payphones to unblock access to alternative OSPs through the use of access codes (including 800 access numbers), PSPs cannot block access to toll free numbers generally. However, TOCSIA does not prohibit an IXC from blocking subscriber 800 numbers from payphones, particularly if the IXC wants to avoid paying the per-call compensation charge on these calls. This uneven bargaining between parties

necessitates the Commission's involvement. Second, as discussed more fully below, we conclude that each state should, in light of the instant proceeding, examine and modify its regulations applicable to payphones and PSPs, particularly those rules that impose market entry or exit requirements, and others that are not competitively neutral and consistent with the requirements of Section 276 of the Act. We conclude that, for purposes of ensuring fair compensation through a competitive marketplace, states need only remove those regulations that restrict competition, and they need not address those regulations that, on a competitively neutral basis, provide consumers with information and price disclosure. Third, we conclude that callers should have information in every instance about the price of the calls they make from payphones. To this end, we require that each payphone clearly indicate the local coin rate within the informational placard on each payphone.

50. While the most appropriate way to ensure fair compensation is to let the market set the price for individual payphone calls, we conclude that this transition to market-based rates should occur in two phases. Because LECs will terminate, pursuant to Section 276(b)(1)(b), subsidies for their payphones within one year of the effective date of the rules adopted in this proceeding, LECs will not be eligible to receive compensation under Section 276(b)(1)(a) until that termination date. This one-year period before per-call compensation is effective, as discussed below, will be the first phase of implementing the rules adopted in this proceeding. During this first phase, states may continue to set the local coin rate in the same manner as they currently do. States may, however, move to market-based local coin rates anytime during this one-year period. In addition, the states must conduct its examination of payphone regulations during this one-year period to review and remove, if necessary, those regulations that affect competition, such as entry and exit restrictions. IXCs will pay compensation for access code calls and subscriber 800 calls on a flat-rate basis.

In addition, all payphones must provide free access to dialtone, emergency calls, and telecommunications relay service calls for the hearing disabled.

51. In the second phase, which will begin one year after the effective date of rules adopted in this proceeding, LECs will be eligible to receive compensation, and per-call tracking capabilities will be in place. The carriers to whom payphone calls are routed will be responsible for tracking each compensable call and remitting per-call compensation to the PSP. During this second year, which is the first year of per-call compensation (as opposed to flat-rate compensation), the market will be allowed to set the rate for local coin calls, unless the state can show that there are market failures within the state that would not allow market-based rates. In addition, during the second phase, which will be the first year of per-call compensation (after the initial year of flat-rate compensation), to allow us to ascertain the status of competition in the payphone marketplace, we conclude, as discussed below, that IXCs must pay PSPs a default rate of $.35 for each compensable call, which may be changed by mutual agreement. PSPs will be required to post the local coin rate they choose to charge at each payphone. During the second phase, we may review, at our option, the deregulation of local coin rates nationwide and determine whether marketplace disfunctions exist, such as locational monopolies caused by the size of the location with an exclusive PSP contract or the caller's lack of time to identify potential substitute payphones, and should be addressed by the Commission. If we find that the deregulation of local coin rates warrants a modification of our approach due to market failures, we may choose to set a cap on the number of calls subject to compensation from particular payphones to limit the exercise of locational market power. Absent such a finding, at the conclusion of the second phase, the market-based local coin rate at these payphones will be the default compensation rate for all

compensable calls in absence of an agreement between the PSP and the carrier-payor.

52. Ensuring Fair Compensation. Most commenters who address the issue agree with our tentative conclusion that we must provide for compensation for all access code calls, subscriber 800 and other toll-free number calls, including debit card calls. In keeping with our long-term goal to have the market set the compensation amount, we define "fair compensation" above as where there is a willing seller and a willing buyer at a price agreeable to both. For each of these types of calls, the PSP either receives no revenue for originating these calls (i.e., for subscriber 800 and other toll-free number calls), or it is unable to block callers from making such calls (access code calls). The record in this proceeding includes substantial evidence that the number of these types of calls using payphones has proliferated in the past several years. We conclude, therefore, that we must provide for compensation for access code calls and subscriber 800 and other toll-free number calls, whether they are intrastate or interstate in destination.

53. We tentatively concluded in the Notice that we need not provide for compensation for 0+ calls, because independent payphone providers and non-BOC LECs receive compensation through individual contracts with the payphone's presubscribed IXC. We also tentatively concluded that "competition in this area ensures 'fair' compensation for PSPs." The RBOCs contend, however, that because Section 276(b)(3) expressly grandfathers contracts existing before the date of the statute's enactment between the location provider and the presubscribed carrier on many BOC payphones, the BOCs would not otherwise receive any compensation for 0+ calls. They argue that the Commission must ensure fair compensation for 0+ calls that use BOC payphones. We agree and modify our tentative conclusion so that, once the BOCs reclassify their payphones and terminate all subsidies, pursuant to Section 276(b)(1)(B),

they may receive the per-call compensation established by this Order, so long as they do not otherwise receive compensation for use of their payphones in originating 0+ calls. We conclude further that, in the absence of a contract providing compensation to the PSP for intraLATA 0+ calls, the PSP shall be eligible to collect per-call compensation from the carrier to whom the call is routed. We also conclude that when a caller dials "0" and the payphone subsequently translates this digit, unbeknownst to the caller, into an 800 access number (i.e., as a way of presubscribing the payphone to a particular IXC), such a call is not compensable as an access code call, because it does not put the caller into contact with an alternative carrier.

54. We conclude that PSPs should receive compensation for international calls. We conclude that we have authority under Sections 4(i) and 201(b) of the Communications Act of 1934, as amended, to ensure that PSPs are fairly compensated for international as well as interstate and intrastate calls using their payphones in the United States. In addition, as we stated in the Notice, we find no evidence of congressional intent to leave these calls uncompensated under Section 276. We agree with AT&T and other commenters that a payphone performs similar functions, regardless of the destination of the call.

55. Local Coin Calls. As outlined above, we believe that full and unfettered competition is the best way of achieving Congress' dual objectives to promote "competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public." Competition over time will lead to the more efficient placement of payphones, improved payphone service, and lower prices for consumers. To encourage competition in the payphone marketplace, we ensure in this Report and Order that PSPs are fairly compensated for "each and every completed intrastate and interstate call[;]" terminate certain LEC subsidies for payphones; and permit all PSPs, including BOCs, to

negotiate with the location provider regarding the selection of the presubscribed interLATA and intraLATA carriers.

56. Once competitive conditions exist, we believe that the market should set the compensation amount for all payphone calls, including local coin calls. Because we have an obligation under Section 276 to ensure that the compensation for all local coin calls is fair, we conclude that the market should be allowed to set the price for all compensable calls, including a local coin call. We believe this approach is appropriate because, once PSPs are free to enter the market, and once callers are free to choose payphones for their calls, the market will ultimately determine whether a particular payphone is economically viable. According to the record in this proceeding, five states have already deregulated local coin rates. In four of those states, Iowa, Nebraska, North Dakota, and Wyoming, the market-based rate is $.35 per call. In the other deregulated state, South Dakota, the market-based rate is $.25 per call.

57. Historically, however, the rate for the most common type of call -- the local coin call -- has not been set by the market, but has instead been determined by state commissions. In the Notice, we stated that Section 276 of the Act requires the Commission to ensure that the PSP receives fair compensation for each interstate and intrastate call, including local coin sent-paid calls. Section 276 also states that "to the extent that any State requirements are inconsistent with the Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements." We sought comment in the Notice on how we should exercise our jurisdiction under Section 276, and noted that we have a range of options for ensuring fair compensation for local coin calls, including setting a nationwide local coin rate for all calls originated by payphones, establishing specific national guidelines that states would use to establish a local rate that would ensure that all PSPs are fairly compensated and permitting the states

to continue setting the coin rates for local payphone calls according to factors within their discretion.

58. As we stated in the Notice, the Commission recognizes that the states have long had a traditional and primary role in regulating payphones, including setting local call rates paid by end users. This role, however, has been in the context of LECs providing local payphone service as part of their regulated service. Section 276, however, significantly alters the regulatory landscape by requiring that LEC provision of payphone service be on par with independent PSP provision of service. In addition, by mandating that LEC payphones can no longer receive subsidies from basic exchange services, Section 276 greatly changes the way in which states set local coin rates. Further, Section 276(b)(1)(A) gives the Commission both the jurisdiction to ensure fair compensation for local coin calls and the mandate to establish a plan to compensate PSPs on a per-call basis. We also stated our concern in the Notice that "current local rates may not always 'fairly' compensate the PSP for use of its payphone[,]" because the caller may use the payphone at "a subsidized local coin rate[.]" Based on the record in this proceeding, we conclude that a deregulatory, market-based approach to setting local coin rates is appropriate, because existing local coin rates are not necessarily fairly compensatory.

59. We recognize, however, that the competitive conditions, which are a prerequisite to a deregulatory, market-based approach, do not currently exist and cannot be achieved immediately. Many states impose regulations on PSPs, including certain requirements that must be fulfilled before a PSP can enter or exit the payphone marketplace. We conclude that these state regulations are barriers to a fully competitive payphone market, and, therefore, "to the extent that any State requirements are inconsistent with the Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements." In addition, in some locations, because of the size of the

location with an exclusive PSP contract or the caller's lack of time to identify potential substitute payphones, the PSP may be able to charge an inflated rate for local calls based on its monopoly, pursuant to an exclusive contract with the location provider, on all payphones at the location. We conclude that such monopoly arrangements, in the absence of regulatory oversight, could impair competition.

60. Based on these concerns, we conclude that the overall transition to market-based local coin rates should not occur immediately. As discussed below, LECs will not be required to terminate, pursuant to Section 276(b)(1)(b), certain subsidies associated with their payphones until April 15, 1997. LECs will not be eligible to receive per-call compensation under Section 276(b)(1)(a) for one year, when all such subsidies are terminated. For this one-year period, the states will be responsible for both ensuring that PSPs are fairly compensated for local coin calls and protecting consumers from excessive rates. Eventually, when fully competitive conditions exist, the marketplace will address both concerns. We conclude that, during this one-year period before per-call, as opposed to flat-rate, compensation becomes effective, states may continue to set the local coin rate in the same manner as they currently do. States may, however, move to market-based local coin rates anytime during this one-year period, and are encouraged to do so. In addition, we conclude that during the same period, the states should take additional action to ensure that payphone competition is promoted. As discussed above, we believe that ease of entry and exit in this market will foster competition and allow the market, rather than regulation, to dictate the behavior of the various parties in the payphone industry. To this end, each state should examine and modify its regulations applicable to payphones and PSPs, removing, in particular, those rules that impose market entry or exit requirements. We conclude that, for purposes of ensuring fair compensation through a competitive marketplace, the states should remove only those regulations that affect

payphone competition; the states remain free at all times to impose regulations, on a competitively neutral basis, to provide consumers with information and price disclosure. In addition, the states at all times must ensure that access to dialtone, emergency calls, and telecommunications relay service calls for the hearing disabled is available from all payphones at no charge to the caller.

61. At the conclusion of this first one-year period, the market will be allowed to set the price for a local coin call, as discussed more fully above. However, we conclude that we should make an exception to the market-based approach for states that are able to demonstrate to the Commission that there are market failures within the state that would not allow market-based rates. Such a detailed showing could consist of, for example, a detailed summary of the record of a state proceeding that examines the costs of providing payphone service within that state and the reasons why the public interest is served by having the state set rates within that market. In addition, under our deregulatory, market-based approach, when states have concerns about possible market failures, such as that of payphone locations that charge monopoly rates, they are empowered to act by, for example, mandating that additional PSPs be allowed to provide payphones, or requiring that the PSP secure its contract through a competitive bidding process that ensures the lowest possible rate for callers. If a market failure persists after such action, the state should recommend the matter to the Commission for possible investigation. In addition, during the second phase, after the initial year of flat-rate compensation, we may review, at our option, the deregulation of local coin rates nationwide and determine whether marketplace disfunctions, such as locational monopolies where the size of the location or the caller's lack of time to identify potential substitute payphones, exist and should be addressed by the Commission. At this point, if we find that the deregulation of local coin rates warrants a modification of our approach due to market failures, we may

choose, for example, to set a cap on the number of calls subject to compensation from particular payphones to limit the exercise of locational market power. Absent such a finding, at the conclusion of the second phase, the market-based local coin rate at these payphones will be the default compensation rate for all compensable calls in absence of an agreement between the PSP and the carrier-payor.

62. With regard to "411" directory-assistance calls, we noted that, while incumbent LECs in many jurisdictions currently do not charge the payphone caller for "411" calls made from their own phones, the LECs charge independent payphone providers for directory-assistance calls made from their payphones, and are not always allowed by the state to pass those charges on to callers. We conclude that we must ensure fair compensation for "411" and other directory assistance calls from payphones by permitting the PSP to charge a market-based rate for this service, although a PSP may decline to charge for this service if it chooses. In addition, to help ensure that a LEC does not discriminate in favor of its own payphones, we conclude that if the incumbent LEC imposes a fee on independent payphone providers for "411" calls, then the LEC must impute the same fee to its own payphones for this service.

63. Completed Calls. We agree with the commenters that, because Section 276(b)(1)(A) mandates compensation for "each and every completed intrastate and interstate call," we must determine what constitutes a "completed" call for purposes of per-call compensation. We conclude that a "completed call" is a call that is answered by the called party. We have previously found that, where an 800 calling card call is routed through an IXC's platform, it should not be viewed as two distinct calls -- one to the platform and one to the called party. In addition, in Florida Public Telecommunications Ass'n v. FCC, the United States Court of Appeals for the District of Columbia Circuit emphasized the one-call nature of a subscriber 800 call from

APPENDIX D

RULES AMENDED (IMMEDIATE)

Part 64 of Title 47 of the Code of Federal Regulations is amended as follows:

1. The authority citation for Part 64 is revised to read as follows:

AUTHORITY: Sec. 4, 48 Stat. 1066, as amended: 47 U.S.C. 154, unless otherwise noted. Interpret or apply secs. 201, 218, 226, 228, 276, 48 Stat. 1070, as amended; 47 U.S.C. 201, 218, 226, 228, 276 unless otherwise noted.

2. The heading of Subpart M of Part 64 is revised to read as follows:

Subpart M -- Payphone Compensation

3. The first sentence of Section 64.1301(a) is revised to read as follows:

(a) Each payphone service provider eligible to receive compensation shall be paid $45.85 per payphone per month for originating access code and toll-free calls.

4. Section 64.1301(b) is revised to read as follows:

(b) This compensation shall be paid by interexchange carriers (IXCs) that earn annual toll revenues in excess of $100 million, as reported in the FCC staff report entitled "Long Distance Market Shares." Each individual IXC's compensation obligation shall be set in accordance with its relative share of toll revenues among IXCs required to pay compensation. For example, if total toll revenues of

IXCs required to pay compensation is $50 billion, and one of these IXCs had $5 billion of total toll revenues, the IXC must pay $4.585 per payphone per month.

5. Section 64.1330 is added to read as follows:

64.1330 State Review of Payphone Entry and Exit Regulations and Public Interest Payphones.

(a) Each state must review and remove any of its regulations applicable to payphones and payphone service providers that impose market entry or exit requirements.

(b) Each state must ensure that access to dialtone, emergency calls, and telecommunications relay service calls for the hearing disabled is available from all payphones at no charge to the caller.

(c) Each state must review its rules and policies to determine whether it has provided for public interest payphones consistent with applicable Commission guidelines, evaluate whether it needs to take measures to ensure that such payphones will continue to exist in light of the Commision's implementation of Section 276 of the Communications Act, and administer and fund such programs so that such payphones are supported fairly and equitably. This review must be completed by September 20, 1998.

6. Section 64.1340 is added to read as follows:

64.1340 Right to Negotiate

Unless prohibited by Commission order, payphone service providers have the right to negotiate with the location provider on the location provider's selecting and contracting with, and, subject to the terms of any agreement with the

location provider, to select and contract with, the carriers that carry interLATA and intraLATA calls from their payphones.

7. Section 64.703(b) is revised by removing the "and" at the end of subsection (2); by renumbering subsection (3) as (4); and adding a new subsection (3) as follows: (3) In the case of a pay telephone, the local coin rate for the pay telephone location; and

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS
CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER I--GENERAL PROVISIONS

Current through P.L. 105-41, approved 8-13-97

§ 151. Purposes of chapter; Federal Communications Commission created

For the purpose of regulating interstate and foreign commerce in communication by wire and radio so as to make available, so far as possible, to all the people of the United States, without discrimination on the basis of race, color, religion, national origin, or sex, a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense, for the purpose of promoting safety of life and property through the use of wire and radio communication, and for the purpose of securing a more effective execution of this policy by centralizing authority heretofore granted by law to several agencies and by granting additional authority with respect to interstate and foreign commerce in wire and radio communication, there is created a commission to be known as the "Federal Communications Commission", which shall be constituted as hereinafter provided, and which shall execute and enforce the provisions of this chapter.

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS
CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER I--GENERAL PROVISIONS

§ 152. Application of chapter

(b) Exceptions to Federal Communications Commission jurisdiction

Except as provided in sections 223 through 227 of this title, inclusive, and section 332 of this title, and subject to the provisions of section 301 of this title and subchapter V-A of this chapter, nothing in this chapter shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communication service by wire or radio of any carrier, or (2) any carrier engaged in interstate or foreign communication solely through physical connection with the facilities of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (3) any carrier engaged in interstate or foreign communication solely through connection by radio, or by wire and radio, with facilities, located in an adjoining State or in Canada or Mexico (where they adjoin the State in which the carrier is doing business), of another carrier not directly or indirectly controlling or controlled by, or under direct or indirect common control with such carrier, or (4) any carrier to which clause (2) or clause (3) of this subsection would be applicable except for furnishing interstate mobile radio communication service or radio communication service to mobile stations on land vehicles in Canada or Mexico; except that sections 201 to 205 of this title shall, except as otherwise provided therein, apply to

carriers described in clauses (2), (3), and (4) of this subsection.

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS

CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER II--COMMON CARRIERS
PART I--COMMON CARRIER REGULATION

§ 225. Telecommunications services for hearing-impaired and speech-impaired individuals

(a) Definitions

As used in this section--

(1) Common carrier or carrier

The term "common carrier" or "carrier" includes any common carrier engaged in interstate communication by wire or radio as defined in section 153 of this title and any common carrier engaged in intrastate communication by wire or radio, notwithstanding sections 152(b) and 221(b) of this title.

(b) Availability of telecommunication relay services

(2) Use of general authority and remedies

For the purposes of administering and enforcing the provisions of this section and the regulations prescribed thereunder, the Commission shall have the same authority, power, and functions with respect to common carriers engaged in intrastate communication as the Commission has in administering and enforcing the provisions of this title with respect to any common carrier engaged in interstate communication. Any violation of this section by any

common carrier engaged in intrastate communication shall be subject to the same remedies, penalties, and procedures as are applicable to a violation of this chapter by a common carrier engaged in interstate communication.

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS

CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER II--COMMON CARRIERS
PART I--COMMON CARRIER REGULATION

§ 226. Telephone operator services

(e) Separate rulemaking on access and compensation

(1) Access

The Commission, [FN1] shall require--

(A) that each aggregator ensure within a reasonable time that each of its telephones presubscribed to a provider of operator services allows the consumer to obtain access to the provider of operator services desired by the consumer through the use of an equal access code; or

(B) that all providers of operator services, within a reasonable time, make available to their customers a "950" or "800" access code number for use in making operator services calls from anywhere in the United States; or

(C) that the requirements described under both subparagraphs (A) and (B) apply.

(2) Compensation

The Commission shall consider the need to prescribe compensation (other than advance payment by consumers) for owners of competitive public pay telephones for calls routed to providers of operator services that are other than

the presubscribed provider of operator services for such telephones. Within 9 months after October 17, 1990, the Commission shall reach a final decision on whether to prescribe such compensation.

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS
CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER III--SPECIAL PROVISIONS RELATING TO RADIO
PART I--GENERAL PROVISIONS

§ 332. Mobile services

(c) Regulatory treatment of mobile services

(3) State preemption

(A) Notwithstanding sections 152(b) and 221(b) of this title, no State or local government shall have any authority to regulate the entry of or the rates charged by any commercial mobile service or any private mobile service, except that this paragraph shall not prohibit a State from regulating the other terms and conditions of commercial mobile services. Nothing in this subparagraph shall exempt providers of commercial mobile services (where such services are a substitute for land line telephone exchange service for a substantial portion of the communications within such State) from requirements imposed by a State commission on all providers of telecommunications services necessary to ensure the universal availability of telecommunications service at affordable rates. Notwithstanding the first sentence of this subparagraph, a State may petition the Commission for authority to regulate the rates for any commercial mobile service and the Commission shall grant such petition if such State demonstrates that--

(i) market conditions with respect to such services fail to protect subscribers adequately from unjust

and unreasonable rates or rates that are unjustly or unreasonably discriminatory; or

(ii) such market conditions exist and such service is a replacement for land line telephone exchange service for a substantial portion of the telephone land line exchange service within such State.

The Commission shall provide reasonable opportunity for public comment in response to such petition, and shall, within 9 months after the date of its submission, grant or deny such petition. If the Commission grants such petition, the Commission shall authorize the State to exercise under State law such authority over rates, for such periods of time, as the Commission deems necessary to ensure that such rates are just and reasonable and not unjustly or unreasonably discriminatory.

UNITED STATES CODE ANNOTATED
TITLE 47. TELEGRAPHS, TELEPHONES, AND RADIOTELEGRAPHS

CHAPTER 5--WIRE OR RADIO COMMUNICATION
SUBCHAPTER II--COMMON CARRIERS
PART III--SPECIAL PROVISIONS CONCERNING BELL OPERATING COMPANIES

§ 276. Provision of payphone service

(a) Nondiscrimination safeguards

After the effective date of the rules prescribed pursuant to subsection (b) of this section, any Bell operating company that provides payphone service--

(1) shall not subsidize its payphone service directly or indirectly from its telephone exchange service operations or its exchange access operations; and

(2) shall not prefer or discriminate in favor of its payphone service.

(b) Regulations

(1) Contents of regulations

In order to promote competition among payphone service providers and promote the widespread deployment of payphone services to the benefit of the general public, within 9 months after February 8, 1996, the Commission shall take all actions necessary (including any reconsideration) to prescribe regulations that--

(A) establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone, except that emergency calls and telecommunications relay service calls for hearing disabled individuals shall not be subject to such compensation;

(B) discontinue the intrastate and interstate carrier access charge payphone service elements and payments in effect on such date of enactment, and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues, in favor of a compensation plan as specified in subparagraph (A);

(C) prescribe a set of nonstructural safeguards for Bell operating company payphone service to implement the provisions of paragraphs (1) and (2) of subsection (a) of this section, which safeguards shall, at a minimum, include the nonstructural safeguards equal to those adopted in the Computer Inquiry- III (CC Docket No. 90-623) proceeding;

(D) provide for Bell operating company payphone service providers to have the same right that independent payphone providers have to negotiate with the location provider on the location provider's selecting and contracting with, and, subject to the terms of any agreement with the location provider, to select and contract with, the carriers that carry interLATA calls from their payphones, unless the Commission determines in the rulemaking pursuant to this section that it is not in the public interest; and

(E) provide for all payphone service providers to have the right to negotiate with the location provider on the location provider's selecting and contracting with, and, subject to the terms of any agreement with the location

provider, to select and contract with, the carriers that carry intraLATA calls from their payphones.

(2) Public interest telephones

In the rulemaking conducted pursuant to paragraph (1), the Commission shall determine whether public interest payphones, which are provided in the interest of public health, safety, and welfare, in locations where there would otherwise not be a payphone, should be maintained, and if so, ensure that such public interest payphones are supported fairly and equitably.

(3) Existing contracts

Nothing in this section shall affect any existing contracts between location providers and payphone service providers or interLATA or intraLATA carriers that are in force and effect as of February 8, 1996.

(c) State preemption

To the extent that any State requirements are inconsistent with the Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements.

(d) Definition

As used in this section, the term "payphone service" means the provision of public or semi-public pay telephones, the provision of inmate telephone service in correctional institutions, and any ancillary services.

TITLE V – PENAL PROVISIONS
FORFEITURES

[47 U.S.C. 501] GENERAL PENALTY.

Any person who willfully and knowingly does or causes or suffers to be done any act, matter or thing, in this Act prohibited or declared to be unlawful, or who willfully and knowingly omits or fails to do any act, matter, or thing in this Act required to be done, or willfully and knowingly causes or suffers such omission or failure, shall upon conviction therof, be punished for such offense, for which no penalty (other than a forfeiture) is provided in this Act, by a fine of not more than $10,000 or by imprisonment for a term not exceeding one year, or both; except that any person, having been once convicted of an offense punishable under this section, who is subsequently convicted of violating any provision of this Act punishable under this section, shall be punished by a fine of not more than $10,000 or by imprisonment for a term not exceeding two years or both.

[47 U.S.C. 502] VIOLATION OF RULES, REGULATIONS, AND SO FORTH.

Any person who willfully and knowingly violates any rule, regulation, restriction, or condition made or imposed by the Commission under authority of this Act, or any rule, regulation, restriction, or condition made or imposed by any internation radio or wire communications treaty or convention or regulations annexed therto, to which the United States is or may hereafter become a party, shall, in addition to any other penalties provided by law, be punished, upon conviction thereof, by a fine of not more than $500 for each and every day during which such offense occurs.

PETITION ORIGINALLY ARGUED ON MAY 13, 1997
DECISION ENTERED JULY 1, 1997

In the
United States Court of Appeals
for the
District of Columbia Circuit

Nos. 96-1394 (and consolidated cases)

Illinois Public Telecommunications Association, et al.

Petitioners,

v.

Federal Communications Commission
and United States of America,

Respondents.

PETITION OF VIRGINIA STATE CORPORATION COMMISSION FOR REHEARING AND SUGGESTION FOR IN BANC CONSIDERATION

Robert M. Gillespie
Associate General Counsel

Virginia State Corporation Commission
Post Office Box 1197
Richmond, Virginia 23218
(804) 371-9671
Fax: 371-9240
Counsel for Virginia State
Corporation Commission

August 13, 1997

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

GLOSSARY iv

ARGUMENT 1

I. CONCISE STATEMENT OF ISSUES AND THEIR IMPORTANCE 1

II. COMPENSATION DOES NOT EQUATE TO PRICE SETTING 2

III. IN LIGHT OF PRINTZ, THE FCC'S INTERPRETATION VIOLATES THE 10TH AMENDMENT BY IMPRESSING STATE OFFICIALS TO IMPLEMENT THE FEDERAL COMPENSATION PLAN 4

CONCLUSION 5

CERTIFICATE OF SERVICE 6

ADDENDUM A -- PER CURIAM DECISION

ADDENDUM B -- EXCERPTS OF TRANSCRIPT OF MAY 13, 1997

ORAL ARGUMENT

TABLE OF AUTHORITIES

Cases

Louisiana Public Service Commission v. FCC,
476 U.S. 355, 106 S.Ct. 1890,
90 L.Ed.2d 369 (1986) MAY 13, 1997 2

New York v. U.S., 505 U.S. 114, 112 S.Ct. 2408,
120 L.Ed.2d (1992) 4

Printz v. U.S., _U.S.__, 117 S.Ct 2365,
65 U.S.L.W. 4731 (June 27, 1997) 1,4

STATUTES

47 U.S.C. § 276(b)(1)(A) 1,2

47 U.S.C. § 152(b) 2

47 U.S.C. § 332(C)(3)(A) 3

47 U.S.C. § 276 ..... *passim*

LEGISLATIVE HISTORY

House of Representatives Conference Rep. No 104-458,
104th Cong., 2d Sess. (1996), reprinted in
Telecommunications Act of 1996 Law and Legislative
History at CR-157-158 (1996) 2

ADMINISTRATIVE DECISIONS

Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket Nos. 96-128 and 91-35, No. 96-388, Report & Order (September 20,1996) 1,3,4

Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act 1996, CC Docket Nos. 96-128 and 91-35, No. 96-439, Order of Reconsideration (November 8,1996) ..... *passim*

GLOSSARY

FCC	Federal Communications Commission
LEC	Local Exchange Company
IXC	Interexchange Carrier
PSP	Payphone Station Provider
BOC	Bell Operating Company

I. CONCISE STATEMENT OF ISSUES AND THEIR IMPORTANCE

Various state regulatory commissions sought review of decisions[1] by the Federal Communications Commission ("FCC") preempting traditional state regulation of the price charged for local coin payphone service. The FCC interpreted § 276 of the Telecommunications Act of 1996 as a Congressional directive to assume jurisdiction of this historically intrastate rate. This Court's July 1, 1997 per curiam decision affirmed the FCC's interpretation. The Court held that Congress' granting the FCC the authority to ". . . establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone . . .", 47 U.S.C. § 276(b)(1)(A), was an unambiguous command for the FCC to assume price-setting authority over coin calls. Petitioners suggest that this holding should be reconsidered by the entire Circuit and corrected because compensation does not of necessity entail determination of retail prices and, in light of the Supreme Court ruling in Printz v. U.S., _____ U.S. _, 117 S.Ct. 2365, 65 U.S.L.W. 4731 (June 27, 1997), § 276 of the Act should not be interpreted to commandeer state regulatory commissions to implement the federal compensation plan.

---

[1] In the Matter of Implementation of the Payphone Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket Nos. 96-128 and 91-35, Report and Order (Released Sept. 20, 1996) (hereafter, "Payphone Order") and Order Reconsideration (Released Nov. 8, 1996) (hereafter, "Reconsideration Order")

II. COMPENSATION DOES NOT EQUATE TO PRICE SETTING

Congress did not intend to override state pricing authority over the coin rate. Section 2(b) of the Communications Act of 1934, 47 U.S.C. § 152(b) fences off such intrastate rates from the FCC. In Louisiana Public Service Commission v. FCC, 476 U.S. 355, 106 S. Ct. 1890, 90 L. Ed. 2d 369 (1986), the Supreme Court ruled that the Communications Act of 1934 is not to be interpreted to confer upon the FCC jurisdiction over intrastate rates unless Congress' language is " .... so unambiguous or straightforward so as to override the command of § 152(b)." Id. at 377.

It is submitted that the language quoted above from § 276(b)(1)(A) merely shows Congress' intent that payphone providers no longer have to provide "free" or "uncompensated" use of their instruments when end users place "toll free" telephone calls. See, House of Representatives Conference Report, No. 104-458, 104th Cong., 2d Sess., January 31, 1996, at pp. 158-159. The term "compensation" means to make a suitable or proper payment. Requiring that "compensation be afforded" That broad term does not necessarily include the authority to determine the specific price to be paid for local coin calls and the FCC had to extrapolate in order to find it had jurisdiction over coin charges. See Payphone Order ¶s 57-58. In fact, counsel for the FCC, in reponse to questions from the Court, conceded "compensation" is ambiguous. See Addendum B, Transcript of May 13, 1997 Oral Argument, at pp. 54-65.

Congress can and has used unambiguous and straightforward language to preempt state ratemaking authority. In 1993, it added § 332(c)(3)(A) to the Act to give the FCC exclusive authority over the rates of commercial

mobile service providers. Section 2(b) was overridden as follows:

> Notwithstanding sections 2(b) and 221(b), no State or local government shall have any authority to regulate . . . rates charged by any commercial mobile service .... 47 U.S.C. § 332(c)(3)(A).

The FCC could have accomplished Congress' command to ensure fair compensation without preempting the states by, for example, reviewing the coin rates authorized by the states. If it found some rates uncompensatory, it could have set a national minimum rate without usurping state authority to set coin rates at or above that minimum. The FCC also had the alternative of using a "carrier pays" system to fund any deficiency in coin rates. A "carrier pays" system was adopted to assure compensation to each PSP for IXC (long distance) traffic. That system could have extended to cover any coin deficiency.

III. IN LIGHT OF PRINTZ, THE FCC'S INTERPRETATION VIOLATES THE 10TH AMENDMENT BY IMPRESSING STATE OFFICIALS TO IMPLEMENT THE FEDERAL COMPENSATION PLAN

Just before the per curiam decision herein, the Supreme Court rendered its decision in Printz v. U.S., 120 U.S. 123, 117 S. Ct. 2365, 65 U.S.L.W. 4731 (June 27, 1997). That decision, together with New York v. U.S., 505 U.S. 144, 112 S. Ct 2408, 120 L.Ed.2d 120 (1992), made it clear that under principles of federalism, state executive officials and state legislative officials cannot be made to work for the federal government by Congress' decreeing that they enforce or enact federal policy.

Petitioner urges the Court to reconsider the July 1, 1997 decision to eliminate 10th Amendment infirmities embedded in § 276 or brought on by the FCC's interpretation of § 276. Specifically, the FCC Orders require state adminsitrative agencies who regulate telephone service to:

(1) review and remove any regulations applicable to payphones and payphone service providers that impose market entry or exit requirements, Payphone Order at ¶ 50, and

(2) review telephone company tariffs for unbundling of functionalities and the elimination of any cross-subsidies flowing for local exchange service to LEC payphones, Reconsideration Order at ¶ 163.

IV. CONCLUSION

Because there is ambiguity as to Congress' intent to override state regulation of coin rates and because of the importance of the Printz decision, supra, on policies of dual sovereignty and federalism, the Virginia State Corporation Commission respectfully suggests that the entire Court consider this case in banc or that the panel reconsider its decision of July 1, 1997. In either event, the panel's decision on coin rate preemption should be reversed and the FCC's orders remanded or vacated.

Respectfully submitted
Virginia State Corporation Commission

Counsel
Robert M. Gillespie
Associate General Counsel
State Corporation Commission
Office of General Counsel
P.O. Box 1197

Richmond, Virginia 23218
(804) 371-9671

August 13, 1997

IN THE
UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

THE ILLINOIS PUBLIC	§
TELECOMMUNICATIONS ASSOCIATION	§
	§
Petitioner	§
CASE NO. 96-1394	
v.	§
(And Consolidated Cases)	
	§
FEDERAL COMMUNICATIONS	§
COMMISSION	§
	§
Respondent	§

PETITION FOR REHEARING AND SUGGESTION FOR REHEARING IN BANC OF CONSUMER INTERVENORS: TEXAS OFFICE OF PUBLIC UTILITY COUNSEL AND CONSUMER FEDERATION OF AMERICA

SUZI RAY McCLELLAN
RICK GUZMAN
EVA KING ANDRIES
P.O. Box 12397
Austin, Texas 78711-2397
(512) 936-7500

Counsel for and on Behalf of:
TEXAS OFFICE OF PUBLIC UTILITY COUNSEL
CONSUMER FEDERATION OF AMERICA

Dated: August 11, 1997

TABLE OF CONTENTS

TABLE OF AUTHORITIES i

ARGUMENT

I. CONCISE STATEMENT OF ISSUE AND ITS IMPORTANCE 1

II. POINT OF ERROR NO. 1 -- The Panel Erred In Upholding The Validity Of The FCC Payphone Order, Because It Did Not Consider That §276 As Implemented By The FCC Explicitly Requires The Sovereign States As States To Enforce Certain Federal Policies. The FCC Order, Thus, Converts The State Commissions Into Federal Field Offices In Violation Of The Tenth Amendment And Principles Of Dual Sovereignty 3

III. POINT OF ERROR NO. 2 – The Panel Erred In Upholding The Validity Of The FCC Payphone Order, Because By Finding That The Congress Authorized The FCC To Regulate The Local Coin Rate, The Panel Did Not Consider That §276 In Inconsistent with the Commerce Clause ..... .10

CONCLUSION ..... .15

CERTIFICATE OF SERVICE

ADDENDUM A — PANEL OPINION

ADDENDUM B – STATUTES AND REGULATIONS

TABLE OF AUTHORITIES

CASES

Federal Energy Regulatory Commission v. Mississippi, 102 S. Ct. 2126 (1982).

Garcia v. San Antonio Metropolitan Transit Authority, 105 S. Ct. 1005 (1985).

Iowa Utilities Board v. FCC, No. 96-3321 (8th Cir. July 18, 1997).

Louisiana Public Service Commission v. FCC, 106 S. Ct. 1890, 1899 (1986).

Lowry v. Bankers Life and Casualty Retirement Plan, 871 F.2d 522 (5th Cir. 1989), *cert. denied*, 114 S. Ct. 682.

New York v. U.S., 112 S. Ct. 2408 (1992).

Printz v. Mack, 65 U.S.L.W. 4731 (U.S. June 27, 1997).

U.S. v. Lopez, 115 S. Ct. 1624 (1995).

West Lynn Creamery Corp. v. Healy, 114 S. Ct. 2205 (1994).

Wickard v. Filburn, 63 S. Ct. 82 (1942).

AGENCY DECISION

In the Matter of the Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 Report and Order (FCC 96-388, released September 20, 1996) [Payphone Order].

STATUTES AND REGULATIONS

Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 *to be codified at* 47 U.S.C. §§ 151 *et. seq.* (1996) ("Telecom Act" or the "Act") (all citations to the 1996 Act will be to the Act as codified in the United States Code).

Public Utility Regulatory Act of 1995, TEX. REV. CIV. STAT. ANN. Art 1446c-o §3.2625 (Vernon Supp. 1997) [PURA95].

Texas Public Utility Commission Substantive Rule §23.54(g), 16 Tex. Adm. Code §23.54(g).

OTHER AUTHORITIES

H.R. Rep. No. 204, 104th Congress, 1st Session (1995).

On Review of an Order of the Federal Communications Commission

PETITION FOR REHEARING AND SUGGESTION FOR REHEARING IN BANC OF CONSUMER INTERVENORS: TEXAS OFFICE OF PUBLIC UTILITY COUNSEL AND CONSUMER FEDERATION OF AMERICA

Pursuant to Federal Rule of Appellate Procedure Nos. 35 and 40 and the D.C. Circuit Local Rules, Consumer Intervenors-Texas Office of Public Utility Counsel (Texas OPC) and the Consumer Federation of America (CFA) - respectfully submit this Petition for Rehearing and suggestion for rehearing *en banc*. Consumer Intervenors seek rehearing on the following points of law, which Petitioner contends the Panel has overlooked:

I.
CONCISE STATEMENT OF ISSUE AND ITS IMPORTANCE

Congress specifically required the FCC to "establish a per call compensation plan to ensure that all payphone service providers are *fairly* compensated for each and every completed intrastate and interstate call using their payphone." Payphone Order ¶59-60; § 276(b)(1)(A) (emphasis added). The Panel, however, approved of the FCC's interpretation of this statutory language to include the authority to regulate (or deregulate as in this case) local coin calls. The Panel relies on the term "compensation" including the "local coin rate" to reach its conclusion that Congress gave the FCC authority to deregulate local coin call rates in order to achieve the Telecom Act's goals, but the issue of whether §276 itself is consistent with Tenth Amendment jurisprudence was not addressed directly.1 *Illinois Public Telecommunications Assoc.*, slip op at 11-12.

The Panel's decision does not recognize certain constitutional infirmities in the Order raised as a result of a recent Supreme Court decision. *Printz v. Mack*, 65 U.S.L.W. 4731 (U.S. June 27, 1997) (holding Brady Handgun Violence Prevention Act requirement that local law enforcement personnel must conduct background checks is unconstitutional because it violates the Tenth Amendment, separation of powers, and principles of dual sovereignty).

Moreover, the Panel finds that "there is no indication that the Congress intended to exclude local coin rates from

---

1 A related issue is raised by this interpretation of §276(b). If Congress expressly mandated that the FCC implement these particular provisions of the Telecom Act, then under the delegation doctrine the FCC does not have authority, given Congress' mandate, to place responsibility for §276 implementation upon the states.

the term 'compensation' in §276." The Panel then concludes, "the statute unambiguously grants the Commission authority to regulate the rates for local coin calls." *Illinois Public Telecommunications Association v. FCC*, slip op at 11-12. Even if Congress meant to include the phrase "local coin rate" in the §276 term "compensation," that fact still begs the question. For it does not resolve the Commerce Clause issue of finding a plain statement by the Congress of the "substantial interstate commerce affects" justifying FCC regulation over this local market. Implementation of a federal act by a federal agency should not be interpreted to intrude upon state' Tenth Amendment authority over local rates. These arguments are appropriate for consideration on petition for rehearing because of their importance and because they involve only matters of law raised by an intervening Supreme Court decision. *Lowry v. Bankers Life and Casualty Retirement Plan*, 871 F.2d 522, 523 n. 1, 525-26 (5th Cir. 1989). Petitioners suggest that the Panel's decision should be reconsidered by the entire Circuit and corrected in light of the *Printz* case's analysis of Tenth Amendment issues and in order to address related Commerce Clause issues.

II. REHEARING POINT OF ERROR NO. 1
The Panel Erred In Upholding The Validity Of The FCC Payphone Order Because It Did Not Consider That §276 As Implemented Violates The Tenth Amendment And Principles Of Dual Sovereignty.

Texas OPC and other consumer intervenors respectfully seek rehearing of this Court's decision. *Illinois Public Telecommunications Assoc. v. FCC*, No. 96-1394 (D.C. Cir. July 1, 1997) (per curiam). Section 276, as implemented by the FCC in the Payphone Order, goes so far

as to require the state regulatory commissions to implement certain federal policies as state regulation. The FCC Order, as implemented, thus, converts the state commissions into federal field offices in violation of the Tenth Amendment and principles of dual sovereignty, as articulated in the *Printz* case.

The U.S. Constitution provides that "[t]he powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." U.S. Const., Amdt. 10. This Amendment implicates two concerns, either of which may serve as grounds for attacking suspect federal legislation: separation of powers and political accountability. Considering the first ground, the key question in determining if a federal act, such as the FCC Payphone Order, violates the Tenth Amendment is whether the federal government seeks to regulate the states as states.2

The Supreme Court's most recent decision interpreting Tenth Amendment issues occurred just a few days before the D.C Circuit issued its decision concerning the FCC's payphone order. *Printz v. Mack*, 65 U.S.L.W. 4731 (U.S. June 27, 1997). In the *Printz* case, the Supreme Court determined that the Congress could not directly require local law enforcement officers to conduct background checks, even on an interim basis under the Brady Handgun Violence Prevention Act. The Brady law modified the Gun Control Act of 1968. The Court struck down as

---

2 The test no longer turns on the question of "traditional government functions." *Garcia* overruled the "traditional government functions" Tenth Amendment standard adopted in *National League of Cities v. Usery*, 96 S. Ct. 2465 (1976). *Garcia v. San Antonio Metropolitan Transit Authority*, 105 S. Ct. 1005 (1985) (upholding application of federal minimum-wage and overtime requirements of the Fair Labor Standards Act (FLSA) against the states under a new Tenth Amendment standard).

unconstitutional those provisions of the Brady law that required the chief law enforcement officer of the gun purchaser's residence to "make a reasonable effort to ascertain within five business days whether receipt or possession would be in violation of the law, including research in whatever State and local recordkeeping systems are available and in a national system designated by the Attorney General." 18 U.S.C. §922(s)(2). The Court held that the required background checks were not a proper exercise of Commerce Clause powers because Congress may not compel state officers to execute federal laws, under separation of powers and principles of dual sovereignty. This Court should rehear its decision in order to take into account the Supreme Court's analysis in the *Printz* case, respecting Tenth Amendment issues.

In support, rather than distinguish *New York* (because the federal regulation there was explicitly directed against the state, and not against government officials, as is the case in *Printz*), the *Printz* Supreme Court reaffirms its decision in *New York v. United States*, 112 S. Ct. 2408 (1992). *Printz v. Mack*, 65 U.S.L.W. 4731, 4742 (U.S. June 27, 1997). *New York* holds that principles of federalism are "violated by a formal command from the National Government directing the State to enact a certain policy." *U.S. v. Lopez*, 115 S. Ct. 1624, 1642 (1995) (KENNEDY, J., concurring). Printz, however, expands upon *New York* by forbidding even arguably ministerial acts to assist the federal government in enforcing its law. Furthermore, the *Printz* case struck down federal law even though the background check requirement simply directs local officials to assist the federal government in the implementation of federal law and did not explicitly require state legislatures to make policy (which would have represented an even more egregious action).

The FCC's rules are similar. Payphone Order at ¶¶48-50, 60, and at Appendix D (adding 47 C.F.R. 64.1330). The FCC expressly mandated state review of payphone entry and

exit regulations and public interest. The FCC required as follows:

(a) Each state *must* review and remove any of its regulations applicable to payphones and payphone service providers that impose market entry or exit requirements.

(b) Each state *must* ensure that access to dialtone, emergency calls, and telecommunications relay service calls for the hearing disabled is available from all payphones at no charge to the caller.

(c) Each state *must* review its rules and policies to determine whether it has provided for public interest payphones consistent with applicable Commission guidelines, evaluate whether it needs to take measures to ensure that such payphones will continue to exist in light of the Commission's implementation of Section 276 of the Communications Act, and administer and fund such programs so that such payphones are supported fairly and equitably. This review must be completed by September 20, 1998.

Payphone Order at ¶¶48-50, 60, and at Appendix D (adding 47 C.F.R. 64.1330) (emphases added). Given the mandatory language of this regulatory section, no discretion is left to the states whether to apply federal standards as state policy. Integral to the FCC's deregulation of the local coin rate, and not severable from the bulk of the Order, was the FCC's conclusion that each state should review its existing regulations and modify them in accordance with the new deregulatory policies adopted under authority of the Telecom Act. The subsequent state review was critical to accomplishment of the FCC's new policy. The FCC concluded, "states should take additional action to ensure that payphone competition is promoted." Payphone Order ¶60. Section 276, however, requires the FCC, not the states, to implement the payphone competition goals. If the FCC

actually had to do what it has required of the states, then the scope of the Payphone Order might be much narrower. The states, however, are not free to devote their resources elsewhere, such as addressing local concerns over rising local coin rates.

The FCC rules direct the states to assist the FCC in the implementation of new federal policies under the Telecommunications Act. Payphone Order Appendix D (47 C.F.R. 64.1330). The *Printz* case only required the performance of certain discrete, ministerial tasks, and was addressed specifically to individual law enforcement officers, rather than state officials. The FCC rules are more egregious because they require the states to perform more than discrete ministerial tasks and to actively review all existing state regulation and determine whether any of those regulations constitute payphone market entry or exit barriers. This obligation Congress placed upon the FCC, its federal agency. Accordingly, the present case falls squarely within this zone of constitutional infirmity that the Supreme Court has recognized, because the FCC's Payphone Order affirmatively coerces the states to adopt certain federal payphone policies through the state regulatory process, as their own policies.

This aspect of the Panel's decision, that implicitly approves of state policy-making apparatus being enlisted in support of the accomplishment of a federal agency's policies, places states and consumer intervenors in a difficult position. Under the FCC's Payphone Order as approved by the Panel, policy arrived at through legitimate state political processes will be tossed out in order to make room for state implementation of federal policies. States through their legislature have repeatedly relied upon setting reasonable limits on local payphone calls to prevent exorbitant charges being imposed on callers by the payphone providers. *See, e.g.*, Public Utility Regulatory Act of 1995, TEX. REV. CIV. STAT. ANN. Art 1446c-o §3.2625(c) (Vernon Supp. 1997) [PURA95] (providing for Texas commission public interest

review and setting of a local coin rate).[3] State regulation of the local coin rate is simply not designed to advance economic protectionist goals.

The Supreme Court recognizes a zone for state regulation that advances a legitimate local purpose that cannot be adequately served by reasonable nondiscriminatory alternatives. *Cf. West Lynn Creamery Corp. v. Healy*, 114 S. Ct. 2205, 22214 (1994). The FCC has provided no demonstration as to how state regulation of the local coin rate imposes costs upon interstate commerce. For example, the FCC finds that the subsidy (if one exists at all) is funded from basic exchange services. FCC Payphone Order ¶58. As such it imposes no burden on interstate commerce. Moreover, the FCC by deregulating the local coin rate essentially unraveled the efforts of the fifty states to regulate in this area to protect their public welfare. In fact, the FCC recognized, while discussing public interest payphones, that the "states are better equipped than the Commission to respond to geographic and socio-economic factors affecting the need for such payphones that are too diverse to be effectively addressed on a national basis."

---

3 PURA95 §3.2625 provides:

> The commission shall establish a limit on the charge that may be imposed for a pay telephone coin sent-paid call within the local exchange company's toll-free calling area. The commission may also establish a statewide ceiling on the charge that may be imposed by a provider of pay telephone service for local calls which are collect or operator-assisted or paid by credit card or calling card, provided that the commission shall not establish the ceiling at less than the applicable local rates for such calls of any of the four largest interexchange carriers operating in Texas.

PURA95 §3.2625(c). As a result of laws such as this, the Texas Public Utility Commission adopted rules fixing the rates for local coin calls at 25 cents. Texas Public Utility Commission Substantive Rule §23.54(g), 16 Tex. Adm. Code §23.54(g).

Payphone Order ¶278.

The D.C. Circuit should now reconsider its decision because the *Printz* case, discussed earlier, expands upon the Tenth Amendment doctrine laid down earlier in the *New York* case. *New York v. U.S.*, 112 S. Ct. 2408 (1992). In the *New York* case, the Supreme Court made it clear that state legislatures are not subject to federal direction. *New York*, 112 S. Ct. at 2429 (1992) (Court struck down certain coercive 'take title" provisions of the Low-Level Radioactive Waste Policy Act, requiring states to either take title to waste or regulate according to federal standards, as violations of the Tenth Amendment). The provisions struck down in the *New York* case were found flawed because, among other things, the federal provisions required that "[e]ach State shall be responsible for providing, either by itself or in cooperation with other States, for the disposal of . . . low-level radioactive waste generated within the State." 42 U.S.C. §2021c(a)(1)(A). The take-title provisions required that states "shall take title to the waste, be obligated to take possession of the waste, and shall be liable for all damages . . . as a consequence of the[ir] failure to take possession." 42 U.S.C. §2021e(d)(2)(C).

The FCC's actions in the present case are precisely the type of regulatory decrees that the Court in *New York* was concerned about—direct requirements that the state take certain actions as state regulation per se. As the Court found, Congress has "substantial powers" to compel the nation directly, such that it has no need or ability to require the states to govern according to federal directives. *New York*, 112 S. Ct. at 2421. Furthermore, the present case is distinguishable from the line of cases in which the preempting federal law was upheld because in those cases the federal government only required "consideration of federal standards" by the states and did not "directly compel the States to enact a legislative program." *See FERC v. Mississippi*, 102 S. Ct. 2126, 2140-41 (1982).

The second aspect of Tenth Amendment jurisprudence relates to political accountability issues. Maintaining political accountability touches upon fundamental federal issues, deserving rehearing, because of their importance to the political process. It may well be in the FCC's political interest to not be held responsible to residential and small commercial payphone customers for the inevitable increases to the local coin rate that are expected under the Payphone Order. However, by shifting some of the regulatory burden to the state regulatory agencies, the FCC avoids some of the political accountability associated with its decision. The *Printz* case found political accountability is no less diminished because the federal mandate was directed to state officials rather than to the state per se. The Court held:

> By forcing state governments to absorb the financial burden of implementing a federal regulatory program, Members of Congress can take credit for "solving" problems without having to ask their constituents to pay for the solutions with higher federal taxes. And even when the States are not forced to absorb the costs of implementing a federal program, they are still put in the position of taking the blame for its burdensomeness and for its defects.

Printz v. Mack, 65 U.S.L.W. at 4740.

Because the federal government aggrandizes its regulatory powers by improperly making use of the plenary or police powers of another sovereign entity not subject to the enumerated power limitations set forth in the U.S. Constitution the political accountability of both is diminished. *See New York*, 112 S. Ct. at 2424. This arises because people "perceive the States as 'the immediate and visible guardian of life and property,' a fact which 'contributes more than any other circumstance to impressing

upon the minds of the people affection, esteem, and reverence towards the government." *Garcia*, 105 S. Ct. at 1028 (Justice Powell dissenting). Harm to the states from federal overreaching in this case, therefore, undermines the Constitutional balance of powers designed to ensure Tenth Amendment political accountability.

III. REHEARING POINT OF ERROR NO. 2
The Panel Erred In Upholding The Validity Of The Payphone Order Because Its Interpretation of §276 Is Inconsistent With Commerce Clause Case Law

The Panel relies on the use of the term "compensation" by Congress to include the "local coin rate," based on the use of that term ("compensation") to include enduser rates found in various scattered sections of the Communications Act of 1934, as amended. *Illinois Public Telecommunications Association v. FCC*, slip op at 11-12; *see also* §226(e)(2), §203(c)(1), and §309(j)(2)(A). However, if that is the correct interpretation of §276, then that section violates the Commerce Clause as currently interpreted by the Supreme Court. Unlike the other sections cited by the Panel in its decision, only in §276 is the term "compensation" used in a special way to exercise federal authority over an entirely new area (local coin rate) previously regulated entirely by the states.

The test for determining whether §276 regulation under the Telecommunications Act (or presumably any other section of that Act) represents a proper exercise of Congresses' enumerated powers is whether such regulation properly fits within the Constitution's commerce clause as interpreted by the Courts. *See U.S. v. Lopez*, 115 S. Ct. 1624, 1626-27 (1995) (holding that Gun-Free School Zone Act, making it a federal offense to possess a firearm within a local school zone, exceeded Congress' commerce clause authority,

because possession of firearm in a school zone does not substantially affect interstate commerce).

Under its commerce power, Congress may regulate in three broad categories. First, Congress may regulate "the use of the channels of interstate commerce." *Id.* at 1629. This category is not applicable to §276 regulation. Activity by the states in this area does not even purport to hinder interstate movement, because local coin rates are associated by definition with purely intrastate matters. It is, therefore, not a channel for interstate commerce. Second, Congress may regulate the "instrumentalities of interstate commerce." *Id.* This category is also not applicable to §276 regulation, because unlike the payphone itself, the local coin rate relates to an activity, not an instrumentality of commerce. Third, Congress may regulate "those activities having a substantial relationship to interstate commerce." *Id.* at 1629-30. It is within this category that §276 regulation over the local coin rate falls. Regarding this category, the Supreme Court has recently stated that "the proper test requires an analysis of whether the regulated activity 'substantially affects' interstate commerce." *Id.* at 1630. A court may invalidate legislation enacted under the Commerce Clause only if it is clear that there is no *rational basis* for a congressional finding that the regulated activity affects interstate commerce, or that there is no reasonable connection between the regulatory means selected and the asserted ends. *See FERC v. Mississippi,* 102 S. Ct. at 2134.

Presumably, "substantial affects" arises here under the "aggregation principle" because local coin deregulation *en toto* is a critical component to the larger pro-competitive goals Congress sought to realize for payphone providers in the Telecommunications Act--the accomplishment of which would be in doubt unless the local coin rate was deregulated as well. Such a case parallels *Wickard v. Filburn,* 63 S. Ct. 82 (1942) (the most far-reaching example of Commerce Clause authority over intrastate activity). There the Court

found it proper for the Secretary of Agriculture under the Agricultural Adjustment Act of 1938 to penalize an Ohio farmer for raising a small crop of home-consumed wheat. The farmer who grows and consumes his own crop does not contribute his demand to the marketplace. Thus, the Court found that in the aggregate home consumption of wheat effectively depresses the market price for wheat nationally, because it overhangs the market. *See Lopez*, 115 S. Ct. at 1630.

Unlike the situation with homegrown wheat under the Agricultural Adjustment Act of 1938, regulation of telecommunications has a distinct state regulatory component. As is typical of the telecommunications industry, ratemaking is an activity frequently separated into interstate and intrastate activities in order to facilitate the promotion of federal policies without impinging upon equally important state goals. Other provisions, predating the adoption of the Telecom Act, require separation to occur and establish a joint board of state and federal regulators to execute the separation process. 47 U.S.C. 221(c) and 410(c); *Iowa Utilities Board v. FCC*, No. 96-3321 (July 18, 1997) (8th Cir.) slip op at 110-111. Unlike wheat production, separation is a fact of life in the telecommunications industry.

One might argue that language in the House Report suggests "substantial affect," because Congress wanted to vest control of payphone administration in the hands of the federal government for purposes of setting compensation levels among payphone providers. That language, however, did not go so far as to find that continued state regulation over the local coin rate makes it impossible to fashion a fair compensation scheme and it did not rule out the use by the FCC of means less intrusive than outright deregulation of the states. H.R. Rep. No. 204, 104th Cong., 1st Sess. at 88 (1995) (relevant language adopted by Conference Committee report at S.R. Rep. No. 230, 104th Cong., 2d Sess. at 159 (1995)).

Moreover, this lack of supporting legislative history is especially telling because purported federal legislation over the local coin rate constitutes a sharp break from traditions of the past, supportive of state regulation in this area.

One might also expect the FCC to supply the needed "substantial affects" analysis. However, the FCC does not do this. For example, in the Payphone Order the FCC states, as part of its general discussion of its goals for a competitive payphone marketplace, that "[b]ased on the record in this proceeding, we conclude that a deregulatory, market-based approach to setting local coin rates is appropriate, because existing local coin rates are *not necessarily* fairly compensatory." Payphone Order ¶58 (emphasis added). *See also* ¶59. The local coin rate is a matter of intrastate activity. By this tentative language, however, the FCC never finds that deregulation of a purely intrastate activity is an essential component to payphone providers obtaining fair compensation under federal policies.

The thrust of the FCC's concern here is both that payphone providers want to, but cannot, charge the caller more for a local coin call than 25 cents because of state regulatory caps on the rate for a local coin call and that the regional Bell operating companies (RBOCs) keep the local coin rate artificially low through subsidization of the local coin rate from regulated local services. If the payphone provider could charge whatever he wanted for that call, then the FCC believes that more of a market would exist for payphone providers. But that analysis only addresses the local coin market. That this local market and the interstate market can arguably be separated under federal law did not figure into the analysis. If these two markets can be separated, then presumably there are cannot be "substantial affects" on interstate commerce from continued state regulation of the local coin market.

Moreover, with regards to the exercise of the federal power over states, the Supreme Court requires a plain

statement of intent by Congress to exercise the Commerce power over the intrastate field. *Louisiana Public Service Commission v. FCC*, 106 S. Ct. 1890, 1899 (1986). In the recent Eighth Circuit decision affecting §251-252 of the Telecom Act, the Eighth Circuit elaborated on the *Louisiana* decision, finding that "a statute must both unambiguously apply to intrastate telecommunications matters and unambiguously direct the FCC to implement its provisions." *Iowa Utilities Board*, slip op. at 109 (emphasis in original).

In the present case, while the language at §276(b) plainly directs the FCC to regulate -the second prong- in the area of payphone compensation (it is, in fact, placed in a subsection entitled "Contents of Regulations"), there is no separate statutory language that makes it plain that Congress intended §276 to "unambiguously apply" –the first prong- to state regulation over the local coin rate. The use of prior federal enactments (such as the statutory sections from the Communications Act of 1934 cited by the Panel in support of its view that §276 applies to the local coin rate) to supply the needed legislative intent finding are inappropriate because they do not speak contemporaneously to the subject matter or its relationship to interstate commerce. *Lopez*, 115 S. Ct. at 1632.

Courts have an enormous stake in the stability of Commerce Clause jurisprudence as it has evolved to this point. *Lopez*, 115 S. Ct. at 1637 (Justice Kennedy concurring). For this reason, Consumer Intervenors respectfully seeks rehearing on the Panel's decision.

CONCLUSION

The Consumer Intervenors respectfully requests that this Petition for Rehearing and Suggestion for Rehearing en banc be granted, and that Consumer Intervenors be granted such other and further relief as the Court deems just and

proper.

August 11, 1997

Respectfully submitted,

_____

Eva King Andries
On behalf of
Consumer Intervenors

TEXAS OFFICE OF PUBLIC UTILITY COUNSEL
Suzi Ray McClellan
Rick Guzman
Eva King Andries
P.O. Box 12397
Austin, Texas 78711-2397
(512) 936-7500

CONSUMER FEDERATION OF AMERICA
1424 16th Street, NW
Washington, D.C. 20036
(202) 387-6121